No. 80-442

Supreme Court, U. S.
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In the Supreme Court of the United States

OCTOBER TERM, 1980

BEN F. GARMAN,

Petitioner,

vs.

THE NORTHERN TRUST COMPANY,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED[1]

1. Whether a defendant whose motion for dismissal under Rule 41(b) of the Federal Rules of Civil Procedure, made at the close of Plaintiff's presentation of his case at trial, is granted, is denied due process of law when an appellate court reverses the dismissal order and does not remand for further proceedings to allow the defendant to present his case in chief or any of his evidence in defense.

2. Whether the Court of Appeals exceeded its scope of review in not applying a clearly erroneous standard and in determining the credibility of witnesses and questions of intent where the trial court made no such determination.

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[1] Petitioner requests to reserve the right to raise the issue of the Court of Appeals interpretation of reliance in Section 17(a)(2) of the Bankruptcy Act, 11 U.S.C. §35(a)(2), though not a basis for this Petition.

INDEX

PAGE

Opinion below 1

Jurisdiction 2

Statutory provisions involved 2

Statement of the case 3

Reasons for granting the writ 5

1. The decision below conflicts with the explicit language of Rule 41(b) of the Federal Rules of Civil Procedure and Procedural Due Process 5

2. The decision below conflicts with the decisions of other courts of appeals as to the procedure following a reversal of a dismissal order 8

3. The decision below raises significant problems in the scope of review of Appellate Courts and the practice of using Rule 41(b) by defendants 9

Conclusion 12

Appendix:

Opinion and Judgment of Court of Appeals ....App. 1

Denial of petition for rehearing .....App. 19

Memorandum Opinion of District Court .....App. 21

PREVIOUS PAGE WAS BLANK

CITATIONS

PAGE

CASES:

Bach v. Friden Calculating Machinery Company, 148 F2d 407 (6th Cir. 1945) 6

Baltimore & O.R. Co. v. United States, 298 US 349, 80 Led 1209, 56 S Ct 797 (1936) 6

Banks v. Siegel, 181 F2d 309 (4th Cir. 1950) 11

Byrd v. Blue Ridge Rural Electric Cooperative Inc., 356 US 525, 1 L ed 2d 953, 78 SCt 893, reh.den. 357 US 933, 2 Led 2d 1375, 78 S Ct 1366 (1958) 7

Criscuolo v. United States, 250 F2d 388 (7th Cir. 1957) 9

Federal Deposit Ins. Corporation v. Mason, 115 F2d 548 (3rd Cir. 1940) 8

Graver Tank and Mfg. Co. v. Linde Air Products Co., 336 US 271, 93 Led 672, 69 S Ct 535 (1949) 9, 11

Gulbenkian v. Gulbenkian, 147 F2d 173 (2nd Cir. 1945) 8

James Burrough Ltd. v. Sign of the Beefeater, 540 F2d 266 (7th Cir. 1976) 9

Jenkins v. McKeithen, 395 US 411, 23 Led 2d 404, 89 S Ct 1843 (1968) 6

Island Service Company v. Perez, 302 F2d 799 (1972) 9

McKey v. Roetter, 114 F2d 129 (7th Cir. 1940) 8

In Re Oliver, 333 US 257, 92 Led 682, 68 S Ct 499 (1948) 6, 12

Riegel Fiber Corp. v. Anderson Gin Company, 512 F2d 784 (5th Cir. 1975) 9

PAGE

United States v. United States Gypsum Co., 333 US 364, 92 Led 746, 68 S Ct 525 (1948) 7

White v. Rimrock Tidelands, Inc., 414 F2d 1336 (5th Cir. 1969) 8

Whitley v. Powell, 150 F2d 625 (4th Cir. 1946) 9

Zenith Corp. v. Hazeltine, 395 US 100, 23 Led 2d 129, 89 S Ct 1562 (1968) 9

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OCTOBER TERM, 1980

NO.

BEN F. GARMAN,

Petitioner,

VS.

THE NORTHERN TRUST COMPANY,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The petitioner, Ben F. Garman, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered in this proceeding on April 29, 1980.

OPINION BELOW

The opinion of the Court of Appeals for the Seventh Circuit reversing the judgment rendered by the United States District Court for the Northern District of Illinois, Eastern Division entered on April 29, 1980 and not yet reported, appears in the Appendix hereto. The Court of

Appeals denied the petitioner's timely petition for rehearing *en banc* on June 23, 1980. The opinion of the District Court for the Northern District of Illinois, Eastern Division, not reported, appears in the Appendix hereto.

JURISDICTION

The Judgment of the Court of Appeals for the Seventh Circuit was entered on April 29, 1980. A timely petition for rehearing *en banc* was denied on June 23, 1980, and this petition was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

United States Constitution, Fifth Amendment:

"..., nor be deprived of life, liberty or property, without due process of law."

United States Constitution, Fourteenth Amendment, Sec. 1:

"..., nor shall any state deprive any person of life, liberty, or property without due process of law."

United States Code, Title 28 U.S.C. Rule 41(b) Federal Rules of Civil Procedure:

"... After the plaintiff, in an action tried by the court without a jury, has completed the presentation of his evidence, the defendant, without waiving his right to offer evidence in the event the motion is not granted, may move for a dismissal on the ground that upon the facts and the law the plaintiff has shown no right to relief ..."

STATEMENT OF THE CASE

The jurisdiction of the District Court sitting as a Court of Bankruptcy was invoked pursuant to 11 U.S.C. §11 investing such courts with original jurisdiction in proceedings under the Bankruptcy Act (11 U.S.C. 1 *et seq.*). Northern Trust Company, the respondent herein, filed a complaint to determine the dischargeability of the claimed $30,000.00 indebtedness of Ben F. Garman, the bankrupt and petitioner herein, contending that it had relied upon allegedly false financial statements made by the bankrupt, 11 U.S.C. §35(a)(2).

At the trial of the cause, the plaintiff in the proceedings and the respondent herein, called three witnesses to the stand to testify. The first two were its own bank officers, and the third was Ben F. Garman, the petitioner herein, as an adverse witness. These witnesses were cross-examined by the attorney for Ben F. Garman. The following day, without presenting any further evidence, the plaintiff rested its case. Thereupon, without presenting any of its own evidence[2], the defendant immediately moved for an involuntary dismissal pursuant to Rule 41(b) of the Federal Rules of Civil Procedure (28 U.S.C. Fed. Rule 41) which is incorporated into bankruptcy procedure by Bankruptcy Rule 741:

> THE COURT: Do you have anything else?
>
> MR. WEBB: No, Your Honor, the plaintiff rests its case at this time.
>
> THE COURT: All right.

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[2] Though the defendant was able and ready to present its evidence and proceed to offer some 20 exhibits into evidence had the motion been denied (Transcript of Proceedings, p. 6-10, March 28, 1977)

MR. CRANE: Your Honor, at this time the defendant would make a motion for a directed finding based on the—

THE COURT: All right. I would assume so that we have the record proper, you are calling the Court's attention to Rule 41 of the Federal Rules of Civil Procedure which is incorporated into bankruptcy procedure by Bankruptcy Rule 741.

This Rule 41 of the Federal Rules of Civil Procedure provides in sub-part "B" that after the plaintiff in an action tried by the Court without a jury has completed the presentation of his evidence, the defendant without waiving his right to offer evidence in the event that the motion is not granted may move for a dismissal on the ground that upon the facts and law the plaintiff has shown no right to relief.

Why should I grant your motion, Mr. Crane?

(Transcript of Proceedings, p. 4-5, March 29, 1977.)

The Bankruptcy Judge granted defendant's motion and dismissed the complaint. Upon appeal to the District Court, the Bankruptcy Judge's order was affirmed. The Northern Trust Company appealed to the United States Court of Appeals for the Seventh Circuit. There, the Court held that both the Bankruptcy Judge and District Court Judge had placed an "improperly stringent legal standard" upon the plaintiff and reversed the judgment of the District Court. Further, based upon its own findings that the defendant's testimony was "inherently incredible,"[3] the Court remanded the cause for entry of a judgment in favor of the Northern Trust Company. A timely petition for rehearing and suggestion for rehearing *en banc* was denied.

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[3] It should be noted that the portion of the Court of Appeals' Opinion concerning defendant's testimony seems to be largely based upon a deposition which was never offered or admitted into evidence at the trial of the cause. (Transcript of Proceedings, p. 2, March 29, 1977)

REASONS FOR GRANTING THE WRIT

1. THE DECISION BELOW CONFLICTS WITH THE EXPLICIT LANGUAGE OF RULE 41(b) OF THE FEDERAL RULES OF CIVIL PROCEDURE AND PROCEDURAL DUE PROCESS

Rule 41(b) of the Federal Rules of Civil Procedure provides in part:

> After the plaintiff, in an action tried by the court without a jury, has completed the presentation of his evidence, the defendant, without waiving his right to offer evidence in the event the motion is not granted, may move for a dismissal on the ground that upon the facts and the law the plaintiff has shown no right to relief. The Court as trier of the facts may then determine them and render judgment against the plaintiff or may decline to render any judgment against the plaintiff or may decline to render any judgment until the close of all the evidence.

In reliance upon this section, "without waiving his right to offer evidence," Ben F. Garman, the petitioner, moved for an involuntary dismissal of plaintiff's cause, after the Northern Trust Company rested. By reversing the dismissal order and remanding the cause for a judgment to be entered against Ben F. Garman, the United States Court of Appeals has, in effect, waived the defendant's right to offer evidence in direct contravention of the expressed language of Rule 41(b).

By suspending the operation of Rule 41(b) a court of review has placed a party in a worse position than had the motion for dismissal been originally denied. How can

it be said that the due process rights of a party to a fair hearing have been properly protected under such circumstances?

This decision has consequences of great import. If a defendant cannot rely on the expressed language of Rule 41(b), but must fear that a successful motion once reversed may deprive him of presenting his own case, the use of such motion practice shall cease, and the very purpose of Rule 41(b) shall be evaded. This purpose was clearly expressed in *Bach* v. *Friden Calculating Machinery Company,* 148 F2d 407, 410 (6th Cir. 1945).

> "It is clear it was intended by adoption of rules to relieve the defendant in an equity case of the risk of having his proof cut off if he failed on a motion to dismiss at the conclusion of plaintiff's evidence and that it was intended to give that trial court the power to weigh the evidence and draw inferences therefore at the conclusion of plaintiff's proof in both law and equity cases."
>
> . . . If the trial court committed error in this respect, on reversal the defendant clearly would have the right to proceed with the introduction of his evidence under the rule. Any other construction would lack common sense.

This Court has clearly acknowledged the due process rights of a party to a full hearing including the presentation of a defendant's evidence. (*Baltimore & O.R. Co.* v. *United States,* 298 US 349, 368-370, 80 Led 1209, 1224, 56 SCt 797 (1936); *In Re Oliver,* 333 US 257, 273, 92 Led 682, 694, 68 SCt 499 (1948), *Jenkins* v. *McKeithen,* 395 US 411, 429, 23 Led 2d 404, 421, 89 SCt 1843 (1968). Rule 41(b) of the Federal Rules of Civil Procedure specifically provides that a defendant's motion for dismissal does not waive those rights.

It is clear that had defendant, Ben F. Garman's motion been denied, it would have been improper for the trial court to enter a judgment at that time in favor of the defendant; the defendant would still be entitled to present his witnesses and his evidence to refute the plaintiff's case. Thus, the question then becomes whether it is proper for an appellate court to place the defendant in a less favorable position by reversing a dismissal order and directing a judgment in favor of the plaintiff than the defendant would have enjoyed had his motion been denied.

Byrd v. *Blue Ridge Rural Electric Cooperative Inc.*, 356 US 525, 1 Led 2d 953, 78 SCt 893, reh. den. 357 US 933, 2 Led 2d 1375, 78 SCt 1366 (1958), involved a directed judgment for the defendant upon the denial of plaintiff's motion to dismiss an affirmative defense. This Court analogized the situation to a defendant's motion for involuntary dismissal after plaintiff has completed the presentation of his evidence. Where a party relies upon the trial court's view of a statute, though improper, and does not go forward with his proof based on said reliance, he cannot be "penalized by the denial of his day in court to try the issue under the correct interpretation of the statute." (356 US 525, 533).

In *United States* v. *United States Gypsum Co.*, 333 US 364, 401-402, 92 Led 746, 68 SCt 525 (1948), this Court reversed a dismissal order and remanded the cause for further proceedings stating:

> As the order of dismissal came at the end of the government's presentation on appellee's motion to dismiss under Rule 41(b) of the Federal Rules of Civil Procedure, the order is reversed and the case remanded for further proceedings in conformity with this opinion.

2. THE DECISION BELOW CONFLICTS WITH THE DECISIONS OF OTHER COURTS OF APPEALS AS TO THE PROCEDURE FOLLOWING A REVERSAL OF A DISMISSAL ORDER

By its decision in this cause, and its denial of the petition for rehearing in which *McKey* v. *Roetter,* 114 F2d 129 (7th Cir. 1940) was cited as precedence, the Seventh Circuit has placed itself at odds with the position of other circuits.

The Second Circuit has held that where a complaint was erroneously dismissed, the judgment "must be reversed and the cause remanded to afford the defendants an opportunity to offer their evidence." (*Gulbenkian* v. *Gulbenkian,* 147 F2d 173 (2nd Cir. 1945)). The trial would proceed as if the defendant's motion had been denied.

The Third Circuit has also held that a reversal of a dismissal order pursuant to Rule 41(b) is to be treated as though the motion had never been granted. Addressing itself precisely to this point in *Federal Deposit Ins. Corporation* v. *Mason,* 115 F2d 548, 552 (3rd Cir. 1940) the Court stated:

> It is thus seen that if the defendant's motion had not been granted by the district court they would have been entitled to proceed to offer evidence in their defense. Since we now hold that the order granting their motion was erroneous and must be reversed, it follows that the Civil Procedure Rules require that the defendants now be afforded an opportunity to offer their evidence.

Likewise, the Fifth Circuit has held that in such instances the action "must be remanded for further proceedings to allow the defendant to present his case." *White* v. *Rimrock Tidelands, Inc.,* 414 F2d 1336, 1340 (5th Cir.

1969). Nor does it matter that one of the defendants testify as an adverse witness, the defendants still have a right to offer their evidence should the dismissal order be reversed. (*Riegel Fiber Corp.* v. *Anderson Gin Company,* 512 F2d 784 (5th Cir 1975)).

The dicta from cases in other circuits also is contrary to the Seventh Circuit's Opinion. (*Whitley* v. *Powell,* 150 F2d 625 (4th Cir. 1946); *Island Service Company* v. *Perez,* 302 F2d 799 (9th Cir. 1962). Equally disturbing is the fact that the Seventh Circuit has decided several cases with seemingly inconsistent procedural holdings to the instant matter. (*See Criscuolo* v. *United States,* 250 F2d 388, 389-390 (7th Cir. 1957); *James Burrough Ltd.* v. *Sign of the Beefeater,* 540 F2d 266 (7th Cir. 1976)).

3. THE DECISION BELOW RAISES SIGNIFICANT PROBLEMS IN THE SCOPE OF REVIEW OF APPELLATE COURTS AND THE PRACTICE OF USING RULE 41(b) BY DEFENDANTS.

Does the scope of review of an appellate court encompass determining the credibility of witnesses and limiting the rights of defendants to offer evidence contrary to statutory provisions? Although this Court has advised courts of review against deciding factual issues *de novo* (*Zenith Corp.* v. *Hazeltine,* 395 US 100, 123, 23 Led 2d 129, 148, 89 SCt 1562, 1567 (1968)) and particularly in evaluating testimony drawing credibility into question, *Graver Tank and Mfg. Co.* v. *Linde Air Products Co.,* 336 US 271, 275, 93 Led 672, 676, 69 SCt 535, 537-38 (1949), nonetheless, there are occasions where appellate courts have seen fit to delve into this area. However, this problem is compounded when reviewing a dismissal order entered pursuant to a Rule 41(b) motion. This becomes obvious where, as in the instant cause, the appellate court reviews the testimony of the defendant as an adverse witness and

finds such testimony to be "inherently incredible," though neither of the lower courts so found,[4] and then precludes said defendant from presenting evidence to refute the *prima facie* case made by the plaintiff, by directing the district court to enter judgment against the defendant without further proceedings.

It would seem that the proper scope of review of a dismissal order entered at the close of the plaintiff's case should be limited to a determination as to whether the trial judge's order was clearly erroneous. Where the appellate court determines that the trial judge used an incorrect legal standard, the test should be, under the correct legal standard and weighing the evidence, did the plaintiff make a sufficient case to get past the Rule 41(b) motion. If the answer is in the affirmative, then the cause should be remanded to the trial court to enable the defendant to proceed with his defense.

The importance that this Court clarify the procedure of an appellate court reviewing a Rule 41(b) dismissal order cannot be understated. If the procedure of the Seventh Circuit in the instant cause is condoned, then there will be severe ramifications; defendants will no longer move for a dismissal of the cause of action after plaintiff rests for fear of waiving their rights to present their case.

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[4] The Bankruptcy Judge did not make a finding on the intent of Ben F. Garman, but stated:

> I appreciate Mr. Webb's (Plaintiff's attorney) comments about Mr. Garman's testimony though I think that your comments, Mr. Webb, do not necessarily state that or show that Mr. Garman did have the intent. However, I do not make my judgment on whether there was intent to deceive in this case. I looked more to the conduct of the bank in making the loan of November 1, 1973, in the amount of $30,000 to Mr. Garman. (Transcript of Proceedings, p. 62-63, March 29, 1977)

There was no necessity or good reason for the Court of Appeals to inquire into the credibility of the defendant's testimony in the instant matter. Deference should have been given to the trial judge who could hear and observe the demeanor of the defendant. Courts of review should be particularly reluctant to evaluating the credibility of witnesses (*Graver Tank and Mfg. Co. v. Linde Air Products Co.*, 336 US 271, 275, 93 Led 672, 676, 69 SCt 535, 537-38 (1945)), *Banks* v. *Siegel,* 181 F2d 309, 310 (4th Cir. 1950)).

The results of an appellate court failing to abide by such precautions is evident here; acting as a trial court it determined that the defendant's testimony was "inherently incredible" (a role which has been ascribed as the function of the trial court) and acting as an appellate court it reversed and remanded the case for judgment (the trial court could not have awarded judgment at the close of plaintiff's evidence even if the defendants' testimony was "inherently incredible"). The testimony referred to was the limited testimony of the defendant called as an adverse witness. The full testimony of defendant supported by exhibits, other evidence and witnesses was never presented in the trial court, in reliance on Rule 41(b) which specifically states such motion is made without waiving his right to offer evidence.[5]

The Court of Appeals, by acting as both the trial and appellate court, has effectively deprived the defendant of his procedural due process rights of a fair hearing—one where he could present his evidence and have his day in court. This Court must insure that such rights are not so flagrantly cast aside, whether one is an accused criminal,

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[5] Plaintiff's counsel had stipulated to the foundation of some 20 Exhibits defendant had intended to introduce had his motion been denied. (Transcript of Proceedings, March 28, 1977 pp. 6-10)

bankrupt or general civil litigant. Such half-trial adjudication against a defendant was not envisioned by the legislators in the adoption of Rule 41(b) and gnaws away at the doctrine of procedural due process as frequently expressed by this Court:

> A person's right to reasonable notice of a charge against him, and an opportunity to be heard in his defense—a right to his day in court—are basic in our system of jurisprudence. . . . *In Re Oliver,* 333 US 257, 273, 92 Led 682, 694, 68 SCt 499 (1948).

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Seventh Circuit.

Respectfully submitted,

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APPENDIX

APPENDIX

In the

United States Court of Appeals

For the Seventh Circuit

No. 79-1631

IN THE MATTER OF: BEN F. GARMAN, Bankrupt.

THE NORTHERN TRUST COMPANY,

Plaintiff-Appellant,

v.

BEN F. GARMAN,

Defendant-Appellee.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.
No. 75 B 1111—Hubert L. Will, *Judge.*

Argued February 19, 1980—Decided April 29, 1980

Before CASTLE, *Senior Circuit Judge,* PELL and TONE, *Circuit Judges.*

PELL, *Circuit Judge.* Section 17(a)(2) of the Bankruptcy Act of 1938, 11 U.S.C. § 35(a)(2), provides that an individual's debt shall not be discharged in bankruptcy if that debt or its renewal is the result of money obtained "in reliance [by the creditor] upon a materially false

statement in writing respecting [the debtor's] financial condition made or published . . . with intent to deceive. . . ." This appeal calls upon us to decide, *inter alia*, whether non-dischargeability is appropriate only where the creditor's reliance under § 17(a)(2) is "reasonable."

Ben F. Garman, the bankrupt, a life insurance salesman, had been a customer of the Northern Trust Bank (Northern) in Chicago since 1962. Between December, 1970, and March, 1973, Garman borrowed various sums from the Northern resulting in a total indebtedness on November 1, 1973, of $30,000. On that date, Garman executed a renewal note to the Northern for the entire outstanding amount.

There is direct and unimpeached testimony in the record that the Northern, at least in part, expressly relied upon three financial statements submitted by Garman in making these loans.[1] It is uncontested by Garman that these statements omitted listing approximately $50,000 in "claims" that Garman later listed in his petition for bankruptcy.[2]

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[1] There is no requirement that the creditor place exclusive reliance on the financial statement. Partial reliance is sufficient. *See Carini* v. *Matera*, 592 F.2d 378 (7th Cir. 1979); *Cunningham* v. *Elco Distributors*, 189 F.2d 87 (6th Cir. 1951).

[2] Garman's transactions with the Northern can be summarized in the following schedule:

	Date	Amount	Date of statement relied upon	Amount of claims omitted
1.	12/ 9/70	$ 5,000 (loan)	12/ 8/70	$49,800
2.	12/21/71	$ 4,000 (loan)	12/ 8/70	$49,800
3.	9/ 5/72	$ 7,500 (loan) $ 2,500 (renewal)	12/22/71	$51,170
4.	1/15/73	$15,000 (loan)	12/22/71	$51,170
5.	3/ 2/73	$ 5,000 (loan)	2/27/73	$51,170
6.	11/ 1/73	$30,000 (renewal)	2/27/73	$51,170

These claims, however, are recorded as having arisen prior to the time Garman filed the statements with the Northern. Had these amounts been included as potential liabilities in the statements, they would have substantially reduced Garman's net worth, in some instances to less than zero.

Upon Garman's failure to pay the $30,000 when due in April of 1974, the Northern filed suit against him for this amount in state court. On February 6, 1975, prior to judgment in the state court, Garman filed a voluntary petition in bankruptcy listing as unsecured claims to be discharged the $30,000 debt to the Northern as well as the $50,000 in claims not listed on his financial statements. The Northern filed a complaint to prevent the discharge of the $30,000 debt pursuant to § 17(a)(2), and a hearing was held on the issue before a bankruptcy judge on March 28 and 29, 1977. At the hearing, the Northern introduced the testimony of Charles S. Bishop, a Northern vice-president, who had approved most of the loans to Garman, and Carol King, a loan officer who had approved the November 1, 1973 renewal, regarding their reliance on the Garman statements.[3] The Northern also introduced the various notes and statements signed by Garman. Each financial statement provided that it was "a true and complete statement of my financial condition, and details relating thereto. . . . I agree that if any material change occurs I will immediately notify you, unless you are so notified you may continue to rely upon the statement hereon given." Bishop testified that had he known of the $50,000 in claims omitted from the statements, he would not have made the loans.

---

[3] Although King, unlike Bishop, did not specifically state that she had "relied" upon Garman's filed statements when approving the renewal, she did state she had "reviewed" the statements and Garman's credit file as a whole prior to granting her approval. Her reliance on the statements, which at the very least was a partial basis of her decision, is implicit in her testimony.

Garman, testifying as an adverse witness, conceded that he failed to list the $50,000 in claims on the financial statement, but maintained that the omission did not render the statements false. Our examination of his testimony leaves us with the firm conviction that not only was Garman an evasive witness, but that his testimony was inherently incredible. A few illustrations are sufficient to demonstrate our conclusion. One of the creditors listed on Schedule A-3 of the bankruptcy petition was a Dr. Solomon with the claim stated as being approximately $10,800. Garman's attention was directed to the statement at the bottom of the page of Schedule A-3 that "none of the foregoing indebtedness, listed above, are contingent, liquidated or disputed, unless otherwise stated." When asked about the debt to Solomon which had been listed in the schedule without qualification, Garman responded, "[Y]ou keep referring to a debt. We are talking about unsecured claims. I am not talking about any debt." This was followed by an assertion that when he "signed that statement [he] did not acknowledge that was a debt." The record does not indicate whether he was referring here to the bankruptcy schedule or to the financial statement. Either interpretation, however, would fail of verity. If he was referring to the schedule, it clearly refers to "indebtedness." On the other hand, if he was referring to the financial statements, which were signed in the early 1970's, the Solomon claim was not listed although on the schedule he listed it as having been incurred in October, 1968. When asked specifically about listing this item on the financial statements, he said, "It talks about contingent liabilities, sir. I did not have a contingent liability at that time." When the Solomon matter was pursued further, this non-illuminating colloquy followed:

Q. I will rephrase the question.

Mr. Garman, in examining the financial statements marked as Plaintiff's Exhibit Nos. 2, 4, and 7, could you tell me if, reflected on any one of those financial statements, is this claim of Dr. Solomon that is reflected on the bankruptcy petition, is it reflected on any one of those three financial statements?

A. I'm sorry, I can't answer the question.

I find the discrepancy between claim and liability. This is talking about a liability and this is talking about a claim.

Q. You are not answering my question.

A. I can't answer your question.

THE COURT: That is an answer.

The statement that he could not answer the question was repeated with regard to another item of indebtedness listed on the bankruptcy schedule as having been incurred in February, 1972, even though he was being shown a subsequent-in-time financial statement which clearly did not include the debt. On subsequent references to the financial statements, Garman admitted that items were not listed there but did appear on the bankruptcy schedule, including a $4,000 indebtedness to another bank resulting from various loans extended over the past five years, and a promissory note to an estate for $5,000 which related back to January 1968.

Professing that he was "a student of semantics," Garman periodically stated that he could not answer questions, stating on one occasion, "[Y]ou ask me about debts, on the other hand, you are talking about claims." When examined by his own counsel, Garman, in significant candor, related that it had been made clear to him when he was filing in bankruptcy that possible claims should be listed because once he had filed he could not go back and claim that he had forgotten them. His concern about not having

possible claims discharged in bankruptcy did not extend to an equal disclosure when he was borrowing money from Northern. Garman further testified that the unlisted items on the financial statements were not legal documents, they were just informal agreements, and that he did not feel that the word "debt" did "justice to what was involved here as the listing of a claim." The gist of his testimony with regard to a substantial amount of the unlisted items was that Garman would purchase, or would recommend purchase, of certain investments which would be bought with money from friends, and he would share in 50% of the gains but would be responsible for 100% of the losses. He testified he did not consider these as "debts" although he did concede that the $5,000 promissory note, which was also unlisted on the financial statements, was an exception. In sum, while he considered that he had to list all possible claims on the bankruptcy schedule, he felt no similar compulsion on the financial statements even though an answer was required on "other contingent liabilities." As early as 1970, however, he was aware of this part of the statement because he listed a contingent liability of $37,000 as an indorser on notes. Subsequent statements listed no contingent liabilities.

At the conclusion of the hearing, the bankruptcy judge issued no written findings and made no oral findings regarding the materiality of the omissions in the statements or Garman's intent when he filed the statements. Rather, the bankruptcy judge held that the Northern had failed to establish its entitlement to non-discharge of Garman's debt to it because it had not proved it had "reasonably relied" upon the statements. Although the bankruptcy judge's statements do not make clear whether he was basing his decision on a finding of no actual reliance or of no reasonable reliance, the district court on appeal held, correctly we believe, that "it is clear that the bankruptcy judge's dismissal was predicated upon his findings

of no reasonable reliance."[4] The district judge then affirmed the bankruptcy court, stating: "In addition to the requirement that the creditor actually relied, it is clear that § 35(a)(2) requires that the creditor's reliance must have been reasonable." Viewing what it held to be a finding of fact by the bankruptcy judge, the district court held that the finding that the Northern could not have reasonably relied upon these statements was not "clearly erroneous."

Initially, we note that § 17(a)(2), unlike its successor,[5] does not by its terms require a showing of "reasonable reliance" and requires only a showing of reliance in fact.[6] Nevertheless, Garman relies upon a number of decisions ostensibly requiring a showing of reasonableness. *Carini* v. *Matera*, 592 F.2d 378 (7th Cir. 1979); *Kentile Floors, Inc.* v. *Winham*, 440 F.2d 1128 (9th Cir. 1971);

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[4] As noted above, Bishop's testimony that he actually relied on the statements in making the loans was direct and unimpeached, and the bankruptcy judge stated "there is no reason to doubt anything that Mr. Bishop stated in answer to the questions in my opinion."

[5] Section 523(a)(2)(B) of the Bankruptcy Act of 1978 provides, in relevant part:

> A discharge under . . . this title does not discharge an individual debtor from any debt—for obtaining money . . . or an extension [or] renewal, by—use of a statement in writing—(i) that is materially false; (ii) respecting the debtor's . . . financial condition; (iii) on which the creditor to whom the debtor is liable for obtaining such money . . . or credit *reasonably* relied; and (iv) that the debtor caused to be made or published with intent to deceive. . . . (Emphasis added.)

[6] Whether the new § 523 will be subject to the same interpretation we apply today to § 17(a)(2) is a question that will have to await another day for resolution.

In re: Smith, 424 F.Supp. 858 (M.D. La. 1976); *In re: Adams,* 368 F.Supp. 80 (D.S.D. 1973); *Sweet* v. *Ritter Finance Co.,* 263 F.Supp. 540 (W.D. Va. 1967); *In re: Disbrow,* 20 Colliers Bankr. Cases 1149 (D.Ver. 1979); *In re: Ducote,* 4 Bankr. Ct. Dec. 943 (W.D. La. 1978); *In re: Gibbs,* 9 Colliers Bankr. Cases, 608 (M.D. Fla. 1976); *In re: Arden,* 2 Bankr. Ct. Dec. 204 (D.R.I. 1975); *Cash Finance Service, Inc.* v. *Haisch,* 173 So.2d 851 (La. Ct. App. 1965). We believe, however, Garman misinterprets these cases in arguing that they bar the Northern's requested relief.

Although some of the mentioned cases do, in fact, refer to "reasonable" or justifiable reliance as a requirement under § 17(a)(2), they do not require the court, as was done in the present case, to undertake a subjective evaluation and judgment of a creditor's lending policy and practices. These cases simply stand for the proposition that reasonableness is circumstantial evidence of actual reliance; that is, dischargeability shall not be denied where a creditor's claimed "reliance" on a "financial statement" would be *so* unreasonable as not to be actual reliance at all. The opinions relied upon either state this directly, *e.g., Smith, and see Adams* and *Sweet,* or the lack of actual reliance was implicit in the record. In *Arden,* for example, the court held that the creditor knew the alleged misrepresentation was false at the time the loan was made and therefore could not have "reasonably" relied on the "misrepresentation." The court's decision to allow discharge, furthermore, was based upon its holding that the creditor had failed to prove the debtor's intent to defraud. In *Sweet,* one debtor, the husband, could neither read nor write except to sign his name on the statement filled out and signed by his wife. The entire transaction was completed in "no more than two minutes" and the creditor, although charging 30% interest on a portion of the amounts lent, never asked any questions con-

cerning the listed assets or liabilities. The court noted the creditor was simply "taking advantage of a borrower's ignorance" and held that indications that the creditor was well aware of the unsound financial condition of the debtor yet exercised an "almost studied disregard for the truth . . . is enough in most instances to preclude a later claim by the loan company that its reliance on the false financial statement was reasonable." 263 F.Supp. at 542. In *Kentile Floors,* and *Disbrow,* as in *Sweet,* the creditor possessed information that conflicted with the apparent financial well-being portrayed on the debtor's financial statement. In *Cash Finance,* the statement was all but illegible and the court found that it was "obvious" that the list of debts in the statement was incomplete. In *Ducote,* the money was transferred to the debtor at the same time the first financial statement was submitted, thus indicating that "the loan had already been approved when [the debtor] filed the signed financial statement." 4 Bankr. Ct. Dec. at 944. *See also Gibbs and Sweet, supra.* In *Smith* and *Gibbs,* the debtor was a total stranger to the lender and the "financial statement," which was "nothing more than a typewritten statement on the stationery of the company whose financial status they purported to represent," *id.* at 862, was unsigned by the debtor. In *Carini,* this court simply stated, "And, of course, such reliance must be reasonable" while affirming the district court's finding of reasonable reliance. 592 F.2d at 381.

These cases present factual circumstances far different from the one before us here. Garman, the debtor, was a sophisticated businessman who had a longstanding and apparently successful business relationship with the Northern for many years prior to his default. *See, Carini,* at 381. The financial statements he signed did not on their faces indicate the presence of any material misrepresentations or omissions, showed his net worth well in excess

of the loaned amount, and affirmatively required him to notify the Northern in the event of any material change in his financial condition. *Compare, Disbrow.* Furthermore, the Northern had no information indicating that anything stated in the financial statements might be materially false.[7] In sum, there are no facts presented suggesting that the Northern utilized the financial statement simply as a "perfunctory device to be used to contest discharge, and not used to be relied thereon." 1A Colliers on Bankruptcy, ¶ 17.16 at 1636 n.17 (14th ed., 1979), was simply "burying its commercial head in the sand," *Arden, supra,* at 207, or that the Northern's reliance on the financial statements was so unreasonable as not to be actual reliance at all.

Garman protests, however, that to allow Northern to bar discharge in this case would defeat the well-established principle that the Bankruptcy Act "ultimately favors the debtor who invokes its protection." *In re: Schmelzer,* 350 F.Supp. 429, 435 (S.D. Ohio 1972), *aff'd,* 480 F.2d 1074 (6th Cir. 1973). This would be true, of course, in every case where discharge is denied, yet this has failed to preclude the denial of discharge in cases where § 17(a)(2) applied. We believe the Act was meant to discharge only the *honest* debtor from his debts, *Williams* v. *United States Fidelity & Guaranty Co.,* 236 U.S. 549, 555 (1915), and that the Act should be liberally applied

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[7] Although it is true Garman was in default on at least one of the loans at the time of the November 1, 1973 renewal, this does not necessarily indicate that the financial statement misrepresented his financial condition. This fact might well indicate that it was a poor business decision to grant the renewal at that time in that Garman apparently would be required to sell assets to repay his debt. *See* discussion in text, *infra.* However, whether or not it was a poor business decision is not the proper inquiry. Rather, the proper inquiry is whether the claimed reliance on the financial statement accurately to portray Garman's net worth in excess of the debt was so unreasonable as not to be reliance in fact.

to protect the bankrupt only in those cases where there is no intent to violate its provisions. *In re: Schwartz,* 133 F.2d 216, 217 (7th Cir. 1943); *Cunningham* v. *Elco Distributors,* 189 F.2d 87, 89 (6th Cir. 1951). As was stated by the Supreme Court in *Bruning* v. *United States,* 376 U.S. 358, 361 (1964):

> . . . petitioner [is not] aided by the now familiar principle that one main purpose of the Bankruptcy Act is to let the honest debtor begin his financial life anew. As the Court of Appeals noted, § 17 is not a compassionate section for debtors. Rather, it demonstrates congressional judgment that certain problems . . . override the value of giving debtors a wholly fresh start. (Footnote omitted.)

See also United States v. *Sotelo,* 436 U.S. 268, 278-79 (1977).

The bankruptcy and district judges' analyses of the present case, in fact, illustrate the very problems potentially arising from their interpretation of the above mentioned cases. Indeed, their analyses did not address whether the Northern's reliance *on the statements* was reasonable. Rather, they expressed their judgment on whether the decision *to loan Garman the money* was reasonable.[8] They did not hold that the financial statements

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[8] An excerpt from the transcript of the bankruptcy hearing is indicative:

> The Court: The way I look at reliance if you rely on a piece of paper then it has to be that you are able to make a proper business decision.
>
> * * *
>
> What if I think the person who relied on [the statement] is a complete fool?
>
> * * *
>
> Mr. Webb (Northern's counsel): . . . Therefore, there is no question that the financial statement was relied upon. Now whether or not she should have relied upon it is the question

(footnote continued)

showing Garman's net worth in excess of the loaned amount was inherently unreliable; rather, they were concerned by the fact that the Northern would have based its decision to lend money on the net worth and nature of the assets of the debtor rather than the debtor's income.[9] However,

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(footnote continued)

your honor is asking?

The Court: Yes . . . I say that is *bad judgment.*

* * *

Mr. Webb: But the bank did rely upon it.

The Court: Then I fault their judgment. I fault their reliance . . . and I think that it is bad judgment if they relied upon this, even partially relied upon this.

* * *

The Court: The statement dated 2/27/73 does not justify the renewal or extension of credit to Mr. Garman of $30,000. . . . *It is just bad business conduct.*

* * *

The Court: I find it difficult to impose on Mr. Garman the responsibility of the bank's actions in making these loans where I believe that the various statements supposedly relied upon [by] the bank do not warrant in the court's opinion the extension of the credit. . . .

(Emphasis added.)

[9] At one point the bankruptcy judge stated:

Then I look to the financial statement and I say how can anyone look at this personal financial statement . . . which is the one dated February 27, and say on April 30, 1974 [the due date of the renewal note] Ben F. Garman will be able to pay $30,000.

* * *

Where is he going to get that money? He has $80,000 in—he is not going to sell his house. His cash in the bank, what is he going to do with that? He will keep that. He has life insurance cash value. Okay. On the back of it he says he has a loan of $5,000. Will he get another loan? All right, there is $5,000. He has a car. Is he going to sell his car? His coin collection. Are we going to ask him to sell his coin collection? He probably will not.

A lot, $20,000. I do not know what that lot is, whether it is a new home or an old home.

it is not the court's duty under § 17(a)(2) to second guess a creditor's decision to make a loan or to set loan policy for the creditor. If a lender chooses to let net worth rather than income be the determinative factor in loan decisions, it is not for the court to say that this is bad business policy requiring discharge of the resulting debt in bankruptcy. The present issue for the court is simply whether the bankrupt obtained credit, or a renewal, through the creditor's reliance on a materially false financial statement containing information apparently sufficient to obtain an accurate picture of the debtor's financial condition with regard to a reasonable decisional factor in the loan decision, filed by the debtor with the intent to deceive the creditor. The creditor need establish only its reliance in fact, although its claims to reliance cannot be so unreasonable as to defeat a finding of reliance in fact. Given this reliance, the court, with the benefit of hindsight, should not base its decision regarding discharge on whether *it* would have extended the loan. In the present case, the Northern's financial statement form requested sufficient information to obtain an accurate picture of the debtor's net worth, a reasonable decisional factor in the loan decision. To say the Northern should have looked to Garman's income flow instead of net worth is irrelevant to the § 17(a)(2) issues.

The bankruptcy and district judges were also concerned, however, with the fact that at the time the final renewal was granted on November 1, 1973, the most recent financial statement was more than seven months old. We also note that prior loans were granted in reliance upon financial statements that were slightly more than a year old. Although this fact also may raise questions regarding the business judgment shown in the decision to lend the money, we do not think this time lapse renders Northern's reliance on the statements so unreasonable as not

to be reliance in fact. In *Gerdes* v. *Lustgarden*, 266 U.S. 321 (1924), the debtor submitted a financial statement on January 5, 1920, containing, as in the present case, a statement that he would notify the creditor as to any material changes in his financial condition, and that the creditor could continue to rely upon the statement until so notified. Based upon this representation, the creditor, a bank, advanced funds in October and November 1920 and in February of 1921. Upon the debtor's bankruptcy, the bank moved to avoid discharge of the debt pursuant to § 14(b) of the Bankruptcy Act of 1910. The bankruptcy referee allowed the discharge holding that even if the bank had in fact relied upon the statement, "it had no right to so do, since in view of the financial depression prevailing in 1920, the 'reasonable time' for which the statement remained a 'continuing statement' had expired when the credits were extended." 266 U.S. at 324. The district court reversed, finding that the bank had a right to rely upon the statements, but the court of appeals reversed the district court judgment, holding that the lapse of time rendered the bank's reliance unjustified. The Supreme Court reversed the court of appeals, however, stating:

> The only essentials to the statutory bar . . . are (a) that the written statement was made for the purpose of obtaining credit; (b) that it was materially false; and (c) that credit was obtained upon it. If these are established, the vice inherent in the original falsity of the statement is not remedied by the lapse of time; and if the creditor extends credit upon such a false statement while it is still in force and binding upon the bankrupt, within the time in which he intended it should serve that end, it does not lie in his mouth to say that by reason of extrinsic circumstances the creditor was unjustified in relying upon it. In short, the lapse of time is only material in determining whether credit was extended within the period intended, while

> the statement was still binding on the bankrupt, and whether the creditor in fact extended credit upon the faith of the statement.

266 U.S. at 326.

We hold that the same conclusion is appropriate in the present case. Garman clearly filed the financial statements for the purpose of obtaining credit. The financial statements were materially false when they were filed. Finally, the creditor extended credit upon the faith of the statements.

The district and bankruptcy judges were also concerned, however, with the fact that the Northern took no steps to confirm or verify the information Garman set forth in his financial statements. They found, therefore, that any reliance the Northern placed in these statements was unreasonable. In *Carini, supra,* this court faced a similar contention and rejected it, as we do here. *Carini* involved a creditor who had the opportunity to verify the representations of the debtor's solvency made by the debtor in a written statement, and by the debtor's accountant orally. The creditor declined the opportunity "because he and [the debtor] were like brothers, and even had he seen [the verification], he would not have been able to understand [it]." *In re: Matera,* 436 F.Supp. 947, 949 (E.D. Wis. 1977). Nevertheless, this court affirmed the bankruptcy and district judges' refusal to discharge the debt, stating: "Taking into account . . . the close friendship between the parties, . . . the repetition of the false representations over a six-month span, and the other circumstances prior to the loan, the finding of reasonable reliance is supported by the evidence." 592 F.2d at 381. In the present case, we hold that the failure of the Northern to verify the information contained in Garman's statements was not so unreasonable as to justify a

finding that there was no actual reliance. Garman was a longtime customer of the bank and repeated his alleged misrepresentations over a three-year period. The statements themselves contain no information indicating that further investigation may be required, nor is there any allegation that further investigation would have uncovered the great majority of unlisted claims that were attributable to informal and oral arrangements between Garman and his friends. Furthermore, although a creditor is not entitled to rely upon an obviously false representation of the debtor, this does not require him or her to view each representation with incredulity requiring verification. "The law recognizes a duty of each to refrain from even attempted deceit of another with whom he deals, and the right of the latter to assume he will do so. . . ." *Jacobsen* v. *Whitely*, 138 Wis. 434, 120 N.W. 285, 286 (1909). Absent any facts reasonably indicating verification was necessary, we are not persuaded that the Northern's failure to verify rendered its reliance so unreasonable as to discharge Garman's debt.

One further point deserves mention. On appeal, the district court affirmed, *inter alia*, the bankruptcy judge's determination that because the November 1, 1973 renewal note extinguished all prior notes signed by Garman, the only circumstances to be evaluated under § 17(a)(2) were the circumstances surrounding the last renewal. To adopt such a position, however, is to hold that because the Northern failed to discover Garman's misrepresentation at the time of the renewal, all prior alleged misrepresentations by Garman were excused. This we refuse to do. Although the renewal note did, in fact, result in the repayment of the prior notes for bookkeeping purposes, it is clear that in actuality the "renewal" was exactly what its name implies, an extension of the time in which Garman was required to repay the pre-existing debt. Garman's

counsel acknowledged this when he conceded at the oral argument that the $30,000 renewal and the prior notes were all part of the same loan transaction.

Similarly, the fact that the November 1, 1973, renewal was initiated by the Northern rather than Garman is irrelevant to the instant issue. The fact remains that Garman signed financial statements stating that they could be relied upon until he informed the Northern otherwise. He cannot avoid liability on these statements simply because the Northern found that renewing the debt rather than immediately seeking its judicial remedies was in its interest. The Northern properly pleaded and appealed its contentions regarding the whole of Garman's outstanding debt, and the district court, therefore, improperly limited its review to only those circumstances surrounding the November 1, 1973 renewal.

Having held that the bankruptcy and district judges applied an improperly stringent legal standard in this case in finding that the Northern's reliance was "unreasonable," and therefore did not justify a bar to discharge, we see no reason to rule upon whether the bankruptcy judge's finding that Northern failed to meet the more stringent standard was to be reviewed under the "clearly erroneous" or some other standard. Our determination turns simply on a question of law.

Having thus determined that a reversal is necessary, our only remaining question concerns what course further judicial attention to this case should take. We have already set forth that the elements adverted to in *Gerdes* exist without dispute in the record of this case. The remaining question is the matter of "intent to deceive." We find guidance in *Carini, supra,* 592 F.2d at 380:

> In addition, the courts require a showing of fraudulent intent or moral turpitude on the part of the debtor,

> i.e., an intent to deceive. . . . These questions of knowing or reckless falsehood and intent to deceive are questions of fact, . . . and the bankruptcy court's findings on those issues are conclusive unless clearly erroneous. . . . (Citations omitted.)

Here, of course, we are not aided by a finding on this question of fact. Nevertheless, in view of the inherent incredibility of Garman's testimony, which we have previously noted, the continuing omissions in the context of the representations of completeness in the financial statements, in the words of *Carini, supra* at 380, "were grossly reckless at a minimum . . . Indeed, where, as here, a person knowingly or recklessly makes a false representation which the person knows or should know, will induce another to make a loan, intent to deceive may logically be inferred." *Id.* Here, we discern no reason for further extending the life of this litigation.

Accordingly, the judgment of the district court is reversed and the cause is remanded for the entry of a judgment in favor of the Northern Trust Company. Costs will be assessed against the defendant.

A true Copy:

Teste:

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Clerk of the United States Court of Appeals for the Seventh Circuit

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

June 23, 1980

Before

Hon. Latham Castle, Senior Circuit Judge

Hon. Wilbur F. Pell, Jr., Circuit Judge

IN THE MATTER OF
BEN F. GARMAN,
Bankrupt,

No. 79-1631

THE NORTHERN TRUST CO.,
Plaintiff-Appellant,

vs.

BEN F. GARMAN,
Defendant-Appellee

Appeal from the United States District Court for the
Northern District of Illinois, Eastern Division
No. 75 B 1111
Hubert L. Will, *Judge*

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* Circuit Judge Philip W. Tone was a member of the panel which decided this case. However, Judge Tone resigned as a member of this court effective April 30, 1980.

This case is before the court on the petition for rehearing and suggestion for rehearing *en banc* filed in the above-entitled cause by Ben F. Garman, the defendant-appellee. On consideration of the petition for rehearing the court on its own motion excises and strikes from the opinion the following sentence appearing at pages 5-6 of the original slip opinion:

> As early as 1970, however, he was aware of this part of the statement because he listed a contingent liability of $37,000 as an indorser on notes.

The court further notes a question as having been raised in the petition for rehearing as to the propriety of the judgment of this court in ordering a remand for an entry of a judgment in favor of the Northern Trust Company. For the reasons stated in the opinion of the court, under the circumstances of this case the relief was, and still is, deemed appropriate. For precedent for comparable action in this circuit *see McKey* v. *Roetter* 114 F.2d 129 (7th Cir. 1940), *cert. denied,* 311 U.S. 691.

On further consideration of the petition and suggestion for rehearing *en banc,* no judge in active service having requested a vote thereon and both of the judges on the original panel who are still in active service having voted to deny rehearing, accordingly,

IT IS ORDERED that the aforesaid petition for rehearing be, and the same is hereby, DENIED.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE

BEEN F. GARMAN,
Bankrupt,

NORTHERN TRUST COMPANY,

Plaintiff,

v.

BEN F. GARMAN,

Defendant.

Bankruptcy No. 75 B 1111

MEMORANDUM OPINION

This case is before the Court on plaintiff Northern Trust Company's ("Northern") application for review of an order of the bankruptcy court whereby plaintiff's complaint to determine the dischargeability of a $30,000.00 debt owed to the plaintiff was dismissed. Plaintiff contends that, where the unimpeached testimony of the bank's officers was that they had, in fact, relied upon the bankrupt's allegedly false financial statements in granting loans to the bankrupt, the bankruptcy judge committed clear error in holding that the bank did not reasonably rely upon the bankrupt's financial statements. We disagree, and affirm the bankruptcy court's ruling.

BACKGROUND

Between December 9, 1970 and March 2, 1973, Ben F. Garman borrowed various sums of money from and executed promissory notes in favor of Northern. Specifically, Garman borrowed $5,000 on December 9, 1970; $4,000 on December 21, 1971; $10,000 on September 15, 1972; $15,000 on January 15, 1973; and $5,000 on March 2, 1973. As a result of these loans, as of November 1, 1973, Garman had an unpaid balance of $30,000. On November 1, 1973, Garman executed a $30,000 renewal promissory note evidencing his debt to Northern, payable April 30, 1974.

On February 6, 1975, Garman filed a voluntary petition in Bankruptcy, and listed his $30,000 debt to Northern as an unsecured debt to be discharged. Northern filed a complaint to prevent the discharge of the $30,000 debt, alleging that Garman's debt, under 11 U.S.C. §35(a)(2), should not be discharged because that debt resulted from Northern's reliance upon materially false written financial statements submitted to Northern by Garman in order to obtain the loans totalling $30,000. Specifically, Northern alleged that Garman had, with an "intent to deceive," failed to list certain debts and/or contingent liabilities amounting to between $40,000 and $50,000 on several financial statements used to obtain the loans and particularly a financial statement of February 27, 1973 used to obtain the March 2, 1973 loan. Garman subsequently did list these debts and/or contingent liabilities as unsecured claims on his voluntary bankruptcy petition.

On March 28, 1977, the bankruptcy judge heard the testimony of Northern's witnesses in support of its claim that the $30,000 was not dischargeable under 11 U.S.C. § 35(a)(2). Two bank officers of Northern testified. Charles Seaman Bishop, a vice-president of Northern, testified as to his connection with the loans to Garman of December 8, 1970, December 21, 1971, September 5, 1972,

and January 15, 1973. Carol Ann King, a personal banking officer at Northern, testified as to her connection with the renewal loan to Garman of November 1, 1973. Garman also testified with respect to these loans from Northern and his reasons for failing to list certain debts and/or contingent liabilities on the financing statements which he had submitted to Northern.

At the conclusion of the plaintiff's case, Garman moved pursuant to Bankruptcy Rule 741, which incorporates Federal Rules of Civil Procedure 41(b) as applicable to bankruptcy proceedings, for dismissal on the ground that plaintiff had shown no right to relief. The bankruptcy judge granted Garman's motion on the ground that Northern's officer could not have reasonably relied upon Garman's earlier financial statements in making the $30,000 renewal loan on November 1, 1973.[1] In his oral statement

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[1] The bankruptcy judge stated:

> However, I do not make my judgment on whether there was intent to deceive in this case. I looked more to the conduct of the bank in making the loan of November 1, 1973, in the amount of $30,000 to Mr. Garman.
>
> As I review the various exhibits that have been admitted into evidence, particularly the personal financial statements, Plaintiff's Exhibits 2, 4, and 7, I can only surmise that the bank was digging a hole for itself; that the bank could not have reasonably relied on the statements that were filed with the bank.
>
> As to the statement Exhibit No. 2 which is dated December 8, 1970, the bank at that time made a loan to Mr. Garman in the amount of $5,000.
>
> Without much change in the financial worth the bank permitted Mr. Garman for some reason, and I say that reason was not reliance on this statement of financial condition, permitted Mr. Garman to have credit in the amount of $30,000.
>
> Whether prompt action by the bank prior to November 1, 1973, would have avoided a loss to the bank I do not know.

(footnote continued)

of reasons for dismissing Northern's complaint, the bankruptcy judge specifically noted that he did not rule on the issue of whether Northern had made a *prima facie* case as to whether Garman had had the requisite "intent to deceive." The judge also expressed grave doubts, without apparently ruling, that the alleged omissions from the financial statements were not material. The instant appeal followed.

MERITS

In this appeal, Northern argues that the only issue is whether it had established during its case-in-chief that it had relied upon certain false written financial statements submitted to it by Garman in order to obtain the loans. Specifically, Northern argues that numerous cases demonstrate that "a plaintiff alleging non-dischargeability under

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(footnote continued)

> But, I find it difficult to impose on Mr. Garman the responsibility of the bank's actions in making these loans where I believe that the various financial statements supposedly relied upon do not warrant in the Court's opinion the extention [sic] of credit in the manner that has been suggested by the Northern Trust Company.
>
> The materiality of the statements I find rather hard to believe because of my feeling that particularly the statement Exhibit No. 7, the statement dated February 27, 1973, does not justify the renewal or extention [sic] of credit to Mr. Garman of $30,000.

Tr. 62-64, Vol. II. While the judge's statement is susceptible of an interpretation that he found no *actual* reliance, in light of (1) the judge's repeated references to "justify" or "reasonable" in his statements above, (2) the judge's earlier, lengthy inquiry as to whether Northern's reliance upon the February 27, 1973 financial statement was reasonable, Tr. 32-44, Vol. II, and (3) the judge's willingness to accept the fact of King's actual reliance upon the February 27, 1973 financial statement, Tr. 34, Vol. II, it is clear that the bankruptcy judge's dismissal was predicated upon his finding no reasonable reliance on Garman's financial statements in the November 1, 1973 renewal loan.

11 U.S.C. §35(a)(2) sustains his burden of proof as to the reliance element of the statute if there is positive and unimpeached testimony from the lender that he relied upon a written financial statement of the debtor." We disagree.

11 U.S.C. §35(a)(2) provides that a debt of a bankrupt shall not be discharged in bankruptcy if it is a liability:

> for obtaining money or property on credit or obtaining an extension or renewal of credit in reliance upon a materially false statement in writing respecting his financial condition made or published or caused to be made in any manner whatsoever with intent to deceive.
> . . .

Cases construing this statutory provision have held that, among the essential elements for a *prima facie* case under this statute, §35(a)(2) requires that the creditor have actually relied upon the debtor's representations. *In re Matera,* No. 77-2145, Slip Op. at 3 (7th Cir. 1979); *In re Houtman,* 568 F.2d 651, 655 (9th Cir. 1978); *In re Taylor,* 514 F.2d 1370, 1373 (9th Cir. 1975); *Sweet* v. *Ritter Finance Co.,* 263 F.Supp. 540, 543 (W.D.Va. 1967). In addition to the requirement that the creditor have actually relied, it is clear that §35(a)(2) requires that the creditor's reliance must have been reasonable. *In re Matera, supra,* Slip Op. at 3; *In re Smith,* 424 F.Supp. 858, 861-62 (M.D.La. 1976); *In re Adams,* 368 F.Supp. 80, 82 (D.S.D. 1973). As to this requirement that the creditor's reliance have been reasonable, we agree with the statements of the court *In re Arden,* 2 Bank.Ct.Dec. 204 (D.R.I. 1975):

> Sec. 17(a)(2) [11 U.S.C. §35(a)(2)] of the Bankruptcy Act specifically states that extensions or renewals of credit must be made "in reliance upon" false statements. . . .
>
> Though the word "reasonable" does not appear in Sec. 17(a)(2) in connection with reliance, it cannot

> be disputed that reliance must of necessity be reasonable. The element of reasonableness is implicit in the proposition that "[W]hile the Act . . . attempts to strike a balance between the disparate interests involved . . . it must be remembered that the Act ultimately favors the debtor who invokes its protection." *In Re Schmelzer,* 350 F.Supp. 429 (1972), *aff'd,* 480 F.2d 1074 (6th Cir. 1973). . . . It would clearly work against the conscience of this Court to allow recovery by money lenders in cases where their claims are clearly based upon unreasonable reliance.

The burden of proving the reasonableness of the creditor's reliance in a §35(a)(2) suit to prevent discharge must be upon the plaintiff-creditor, as it is with each other element of the plaintiff's case. *See In re Taylor, supra,* 514 F.2d at 1373; *Sweet* v. *Ritter Finance Co., supra,* 263 F.Supp. at 543. Positive and unimpeached statements from the lender's officers as to the lender's actual reliance are not necessarily sufficient, standing alone, to satisfy the plaintiff's burden that its actual reliance was reasonable.

Northern further contends that the bankruptcy judge clearly erred in holding that Northern had unreasonably relied upon Garman's financial statement in making the renewal loan of November 1, 1973.[2] On this appeal, the

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[2] Northern's statement of the issue presented on this appeal is slightly different from our reading of the bankruptcy judge's actual holding. Northern's "Issue Presented for Review" states:

> Did the Bankruptcy Court commit error when it dismissed the Plaintiff's Second Amended Complaint to Determine Dischargeability of Debt at the end of the plaintiff's evidence on the grounds that the plaintiff failed to establish reliance by it upon the defendant-appellee's false written financial statements in making certain *loans* to the defendant-appellee?

Brief for Plaintiff-Appellant, at 1 [emphasis added]. However, it is clear that the bankruptcy judge dismissed plaintiff's complaint

(footnote continued)

bankruptcy court's findings of fact are conclusive unless clearly erroneous. Bankr. Rule 810; *In re Matera, supra,* Slip Op. at 2. Under the circumstances of this case, we find the bankruptcy judge's determination that the plaintiff could not have reasonably relied upon the financial statement submitted by Garman on February 27, 1973 in making the renewal loan of November 1, 1973 to be a finding of fact, and subject, except for the consideration discussed *infra,* to review under the "clearly erroneous" standard of review. *See In re Matera, supra,* Slip Op. at 3 (applied "clearly erroneous" standard to bankruptcy court's determination that creditor reasonably relied). *See also In re Smith, supra,* 424 F.Supp. at 861. *Compare In re Sewell,* 361 F.Supp. 516, 519 (S.D.Ga. 1973).

Notwithstanding our conclusion that the bankruptcy judge's finding of no reasonable reliance is a finding of fact reviewable under the standard of Bankruptcy Rule 810, it is clear from a reading of the transcript that the bankruptcy judge's finding was based primarily upon his

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(footnote continued)
solely on the ground that plaintiff had failed to establish reasonable reliance with respect to the November 1, 1973 renewal loan. Moreover, this ruling of the bankruptcy judge was responsive to plaintiff's theory of the case at trial that it was the circumstances surrounding the $30,000 renewal loan of November 1, 1973 which were determinative of the dischargeability of Garman's $30,000 debt to Northern. Tr. 29-31, Vol. II. On the state of this record, and the narrow holding of the bankruptcy judge that Northern did not reasonably rely upon Garman's financial statements at the time of the November 1, 1973 loan, we construe Northern's appeal as essentially limited to challenging that holding. Accordingly, we do not consider the reasonableness of Northern's reliance upon Garman's written financial statements in making the December 9, 1970, December 21, 1971, September 5, 1972, January 15, 1973 or March 2, 1973 loans as before us on this appeal.

own inspection of the financial statements submitted by Garman, and not upon the live testimony of the three witnesses called by Northern.[3] Under such circumstances, where the judge's findings of fact are based upon documentary evidence, there exists substantial uncertainty in this and other circuits as to whether the "clearly erroneous" standard mandated by Federal Rule 52(a) is still applicable. *See Oscar Gruss & Son* v. *First State Bank of Eldorado,* 582 F.2d 424, 430-31 (7th Cir. 1978). At a minimum, however, under Federal Rule 52(a), findings of fact based on documentary evidence are "entitled to 'some deference' and cannot be set aside unless the appellate court can 'come to a definite and firm conviction that an error [was] committed in the findings.'" *Oscar Gruss & Son* v. *First State Bank of Eldorado, supra,* 582 F.2d at 431, *citing Mercantile National Bank of Chicago* v. *Howmet,* 524 F.2d 1031, 1035 n.3 (7th Cir. 1975), *cert. denied,* 424 U.S. 957 (1976). This statement as to the standard of review for findings of fact based on documentary evidence under Federal Rule 52(a) is equally applicable to the standard of review to be applied by this Court under Bankruptcy Rule 810. *See* Advisory Committee Note to Bankr. Rule 810.

Applying the above standard to the bankruptcy judge's finding that Northern did not reasonably rely upon Garman's financial statements of February 27, 1973 and earlier in making the November 1, 1973 renewal, six-month loan for $30,000, we cannot come to a "definite and firm conviction" that the bankruptcy judge erred. Contrary to

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[3] Bishop, Northern's vice-president who handled several of the pre-November 1, 1973 loans to Garman, testified to the absence of any monthly income and expense information on the financial statements completed by Garman, Tr. 79-81, Vol. I, and that the bank had possibly been "somewhat remiss" in not securing that type of information on its financial statements. Tr. 83, Vol. I.

Northern's assertion that there was nothing on the face of the financial statement nor any testimony from the two bank officers which would indicate that their reliance was unreasonable, several factors persuade us not to overrule the bankruptcy judge.

A review of the information contained on the February 27, 1973 financial statement,[4] which information was supplied by Garman apparently without any independent verification by Northern's officers, reveals that, as of that date, Gaman had net assets of $119,000, a net worth of $58,000, and a gross annual income of $40,000. The vast majority of Garman's assets were in an illiquid form. Moreover, $44,000 of his $58,000 net worth could be attributed to Garman's home (market value less mortgage). With respect to Garman's gross annual income, the financial statement nowhere indicates Garman's aftertax income, nor his estimated monthly income and expenses. Nor does it appear that Garman was asked to furnish such information before November 1, 1973, which information would have given a more accurate indication of his ability to repay a $30,000 loan at the end of a six month period. In addition to the seriously questionable adequacy of the information contained on the February 27 financial statement, it must be remembered that this statement was used some eight months *after* it was written and was used at a time when the bank must clearly have been aware of the problems Garman was having in making payments upon his previous loans. Under such circumstances, we cannot come to a "definite and firm" conclusion that the bank-

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[4] King testified that she had reviewed the February 27, 1973 financial statement prior to the renewal loan of November 1, 1973. Tr. 87-88, Vol. I. She did not testify to having reviewed any other financial statement. Thus, it is essentially the reasonableness of her reliance upon this financial statement which is at issue.

ruptcy judge erred when he concluded both that Northern unreasonably relied upon the February 27 financial statement in renewing the $30,000 loan on November 1, 1973 and that Northern should have taken additional steps to determine whether Garman could, in fact, pay the $30,000.

As previously indicated, the only issue presented to and decided by the bankruptcy judge was the reasonable reliance by Northern on the allegedly false financials in connection with the November 1 renewal and, accordingly, that is the only issue before us.

It is clearly inferable from the fact that Northern obtained no updated financial information in renewing the $30,000 loan on November 1, 1973 that it was not relying on the eight months old and older financial statements at all, but was simply renewing a loan which the borrower was currently unable to repay. Since this inference is consistent with the bankruptcy judge's conclusion, we cannot "come to a definite and firm conviction" that his findings are in error.

Neither case relied upon by Northern is to the contrary. *Household Finance Corp.* v. *Christian,* 98 N.W.2d (Wis. 1959), while procedurally similar to the instant case, is distinguishable. In that case, the court specifically noted that there were no "impeaching circumstances" nor anything "inherently improbable" in the fact that the plaintiff's manager had relied in making a loan upon the defendant's contemporaneous financial statement. 98 N.W.2d at 392, 393. In this case, however, the information contained on the face of the eight month old, February 27 financial statement is enough, in our opinion, to constitute "impeaching circumstances" with respect to Northern's reasonable reliance. *In re Bebar,* 315 F.Supp. 841 (E.D.N.Y. 1970), is inapposite. In *Bebar,* the district court straight-

forwardly applied the "clearly erroneous" standard to affirm a bankruptcy judge's decision resolving a witness credibility issue in favor of the bank officer and against the debtor. No issue was presented in that case with respect to the reasonableness of the bank's reliance upon the debtor's financial statement.

After careful consideration of the record, we cannot come to a "definite and firm" conviction that the bankruptcy judge erred. Accordingly, the bankruptcy judge's order dismissing the plaintiff's complaint must be affirmed.

An appropriate order will enter.

/s/ *Hubert L. Will*
United States District Judge

Dated: April 6, 1979

No. 80-442

In the Supreme Court of the United States

OCTOBER TERM, 1980

BEN F. GARMAN,

Petitioner,

vs.

THE NORTHERN TRUST COMPANY,

Respondent.

BRIEF OF THE NORTHERN TRUST COMPANY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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November, 1980

QUESTION PRESENTED FOR REVIEW

Whether a federal court of appeals has the power to reverse, without remand for a new trial, a Rule 41(b) dismissal entered on behalf of a defendant where the defendant's testimony given as an adverse witness is inherently incredible and where proper resolution of the case is beyond any doubt.

TABLE OF CONTENTS

	PAGE
Opinions Below	1
Jurisdictional Statement	2
Constitutional and Statutory Provisions Involved	2
Statement Of The Case	2
Reasons For Denying The Writ	6
Conclusion	18

Appendix:

Opinion and Judgment of Court of Appeals	App. 1
Transcript of Proceedings in the Bankruptcy Court on March 28, 1977	App. 19

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TABLE OF AUTHORITIES

Cases

PAGE

Albaugh v. Pennsylvania R. Co., 120 F.Supp. 70 (D.D.C. 1954, *aff'd*, 219 F.2d 264 (D.C. Cir. 1955) 12

Becker v. Seaboard Finance Co., 436 F.2d 778 (9th Cir. 1970) 10

James Burrough, Ltd. v. Sign of the Beefeater, Inc., 540 F.2d 266 (7th Cir. 1966) 13

Continental Bank v. Rock Island Ry., 294 U.S. 648 (1935) 13

Crosby v. Buchanan, 90 U.S. (23 Wall.) 420 (1875) 16

Douglas v. City of Jeanette, 319 U.S. 157 (1942) Jackson, J., dissenting) 17

Factor v. CIR, 281 F.2d 100 (9th Cir. 1960), *cert. denied* 364 U.S. 933 (1962) 12

Fisher v. Volz, 496 F.2d 333 (3d Cir. 1974) 17

Geighy Chemical Corp. v. Allen, 224 F.2d 110 (5th Cir. 1955) 12, 13, 15

Gerdes v. Lustigarten, 266 U.S. 321 (1924) 6

Harris v. New York, 401 U.S. 222 (1971) 17

Haynes v. United States, 390 U.S. 85 (1968) 14

Indiana Metal Products v. NLRB, 442 F.2d 46 (7th Cir. 1971) 12

Kostelac v. United States, 247 F.2d 723 (9th Cir. 1957) 13

Kosty v. Lewis, 319 F.2d 744 (D.C. Cir. 1963) 14

Lochner v. New York, 198 U.S. 45 (1905) 15

PAGE

Magna Sales Co. v. Magna Alloys Research Pty., 545 F.2d 668 (9th Cir. 1977) 13

Marin v. England, 385 U.S. 99 (1966) 13

Morgan Guaranty Trust Co. of New York v. Martin, 466 F.2d 593 (7th Cir. 1972) 17

Orloff v. Willoughby, 345 U.S. 83 (1953) 10

Penn Texas Corp. v. Morse, 242 F.2d 243 (7th Cir. 1957) 12

Peters v. Fitzpatrick, 310 F.2d 704 (7th Cir. 1962) ..12, 13

Quock Ting v. United States, 140 U.S. 417-420 (1891) .. 12

Riegel Fiber Corp. v. Anderson Gin Co., 512 F.2d 784 (5th Cir. 1975) 15

Singleton v. Wulff, 428 U.S. 121 (1976) 14

Smith v. Dravo Corp., 208 F.2d 388 (7th Cir. 1953) 13

Thomas E. Snyder & Sons v. Industrial Molasses U.S. 685 (1960) 12

Sun Life Assurance Co. of Canada v. Stacks, 187 F.2d 17 (7th Cir. 1951) 12

In Re Trimble, 55 F.2d 165 (8th Cir. 1932) 11

United States v. Zenith, 395 U.S. 100 (1969) 13

Urban Redevelopment Corp. v. CIR, 294 F.2d 328 (4th Cir. 1961) 12

Walder v. United States, 347 U.S. 62 (1954) 17

In Re West, 158 F.2d 858 (7th Cir. 1946) 11

Wong Ken Foon v. Brownell, 218 F. 2d 444 (9th Cir. 1955) 12

Yunker v. CIR, 256 F.2d 130 (6th Cir. 1958) 13

Constitution, Statutes and Rules

PAGE

Amendment V, Constitution of the United States 4, 17

Bankruptcy Act, 11 U.S.C. §35 U.S.C. §35(a)(2) 2

28 U.S.C. § 2106 .....5, 12, 13, 17

Rule 17, Rules of the Supreme Court of the United States 18

Rule 41(b), Federal Rules of Civil Procedure 4, 7, 15

Rule 52(a), Federal Rules of Civil Procedure 13

Other Authorities

G. Bell, Appellate Court Opinions and the Remand Process, Ga. L. Rev. 526 (1968) 4

J. Cole, Impeachment With Unconstitutionally Obtained Evidence: Coming To Grips With the Perjurous Defendant, 62 Nw. J. C. L. & CRIM. 1 (1971) .. 17

5 J. Moore, Federal Practice §41.13[2] at 41-185 (2d ed. 1980) 14

Note, Individualized Criminal Justice in the Supreme Court: A Study of Dispositional Decision Making, 81 Harv. L. Rev. 1260 (1968) 5

In the Supreme Court of the United States

OCTOBER TERM, 1980

No. 80-442

BEN F. GARMAN,

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vs.

THE NORTHERN TRUST COMPANY,

Respondent.

BRIEF OF THE NORTHERN TRUST COMPANY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

OPINIONS BELOW

The as yet unreported opinion of the United States Court of Appeals for the Seventh Circuit was entered on April 29, 1980. We have reproduced the opinion of the court as an Appendix ("App.") to this brief. *See* App. at 1 through 18, *infra.* The memorandum decision of the United States District Court for the Northern District of Illinois is unreported and is appended to the petition for a writ of certiorari at 21 through 31. The bankruptcy judge for the United States District Court for the Northern District of Illinois did not issue a formal opinion.

JURISDICTIONAL STATEMENT

The jurisdiction of this Court is sought to be predicated upon 28 U.S.C. §1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

1. Amendment V, Constitution of the United States:

   "No person shall be . . . deprived of life, liberty, or property without due process of law. . . ."

2. Rule 41(b), Federal Rules of Civil Procedure:

   "After the plaintiff, in an action tried by the court without a jury, has completed the presentation of his evidence, the defendant, without waiving his right to offer evidence in the event the motion is not granted, may move for a dismissal on the ground that upon the facts and the law the plaintiff has shown no right to relief."

3. 28 U.S.C. §2106:

   "The Supreme Court or any other court of appellate jurisdiction may affirm, modify, vacate, set aside or reverse any judgment, decree, or order of a court lawfully brought before it for review, and may remand the cause and direct the entry of such appropriate judgment, decree, or order, or require such further proceedings to be had as may be just under the circumstances."

STATEMENT OF THE CASE

In early 1975, Mr. Ben Garman ("Garman") filed a voluntary petition in bankruptcy in which he listed a $30,000.00 debt to The Northern Trust Company of Chicago ("the Northern") as an unsecured claim to be discharged. Pursuant to §17(a)(2) of the Bankruptcy Act,[1]

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[1] *See* 11 U.S.C. §35(a)(2).

the Northern filed a complaint to prevent the discharge of this debt on the ground that in granting the loans and renewals it had relied upon materially false and fraudulent written financial statements submitted to it by Mr. Garman.

Following a plenary trial on the issue of dischargeability, the bankruptcy judge held, on March 28, 1977, that the reliance of the Northern was not "reasonable" and dismissed the Northern's complaint. Thereafter, the Northern appealed to the United States District Court for the Northern District of Illinois which held the case for two years before affirming the dismissal on April 6, 1979.[2]

On April 29, 1980, a unanimous panel of the United States Court of Appeals for the Seventh Circuit reversed this judgment.[3] The carefully drafted opinion held, *inter alia,* that reasonableness of reliance under §17(a)(2) of the Bankruptcy Act is not an essential element of a plaintiff's case.[4] The court of appeals expressly reserved for another day resolution of the question of whether §523 of the 1978 Bankruptcy Act will be subject to the same interpretation. *See* App. at 7, n. 6.

After a meticulous review of the record, the court of appeals found that the testimony of Mr. Garman regarding the reasons for his having omitted $50,000.00 in lia-

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[2] The Northern was somehow not notified of the decision and thereafter, inexplicably, the files in the case could not be found in the Clerk's office. As a result, the Northern was forced to obtain permission from the Seventh Circuit to reconstruct the entire record. *See* "Motion of the Northern Trust Company to Reconstruct the Record" (June 14, 1979).

[3] The decision of the Seventh Circuit is appended as an Appendix, at 1-18.

[4] The Petition for Certiorari ("the Petition") does not challenge the validity of this aspect of the Seventh Circuit's decision.

bilities from his various financial statements was "inherently incredible." "[D]iscern[ing] no reason for further extending the life of this litigation," (App. at 18), the court reversed and remanded with instructions that judgment be entered in favor of the Northern.

Following this decision, the petitioner applied to the Seventh Circuit for a rehearing *en banc*. That request was denied without a single dissenting vote. Subsequently, the petitioner moved for issuance of an order staying the mandate in order that he might apply for a writ of *certiorari*. That motion was likewise denied without a single dissenting vote.

The Petition posits that the decision of the court of appeals reversing without remand for a new trial has abridged Mr. Garman's rights under the Due Process Clause of the Fifth Amendment and under Rule 41(b) of the Federal Rules of Civil Procedure. *See* Petition at 5-11. In what follows, we shall demonstrate that the decision of the court of appeals and its disposition of the case were indisputably correct. We shall demonstrate that the decision is not an aberration which has created a conflict among the circuits, but that, on the contrary, the decision is consonant with decisions of every other circuit court of appeals that has been called upon to decide a case with comparable contours.

More than a decade ago, Judge Griffin Bell recognized that "the manner in which an appellate court performs its remand function may go far to lessen the expense and delay in litigation." G. Bell, *Appellate Court Opinions and the Remand Process*, 2 Ga. L. Rev. 526, 537 (1968). "Crowded court dockets and an expanding population accent the need for new and inventive methods and for courts to address their attention to improvements in procedure."

Id. at 527. *Cf.*, Note, *Individualized Criminal Justice in the Supreme Court: A Study of Dispositional Decision Making*, 81 Harv. L. Rev. 1260 (1968). These principles underlie the extraordinarily broad authority vested in federal appellate courts by 28 U.S.C. §2106.[5]

The court of appeals' disposition of the instant case is faithful to the spirit of §2106 and must not be altered by any action of this Court. To do so would be to allow individuals insentive to the basic concepts of truth and honor to play ducks and drakes with the resources of the federal courts.

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[5] Section 2106 provides that:

"The Supreme Court or any other court of appellate jurisdiction may affirm, modify, vacate, set aside or reverse any judgment, decree, or order of a court lawfully brought before it for review, and may remand the cause and direct the entry of such appropriate judgment, decree, or order, or require such further proceedings to be had as may be just under the circumstances."

REASONS FOR DENYING THE WRIT

At the close of its opinion, the Court of Appeals stated:

"Having thus determined that a reversal is necessary, our only remaining question concerns what course further judicial attention to this case should take. We have already set forth that the elements adverted to in *Gerdes* [*v. Lustigarten,* 266 U.S. 321 (1924)] exist without dispute in the record of this case. The remaining question is the matter of "intent to deceive." We find guidance in *Carini, supra,* 592 F.2d at 380:

> In addition, the courts require a showing of fraudulent intent or moral turpitude on the part of the debtor, i.e., an intent to deceive. . . . These questions of knowing or reckless falsehood and intent to deceive are questions of fact, . . . and the bankruptcy court's findings on those issues are conclusive unless clearly erroneous. . . . (Citations omitted.)

"Here, of course, we are not aided by a finding on this question of fact. Nevertheless, in view of the inherent incredibility of Garman's testimony, which we have previously noted, the continuing omissions in the context of the representations of completeness in the financial statements, in the words of *Carini, supra* at 380, "were grossly reckless at a minimum . . . Indeed, where, as here, a person knowingly or recklessly makes a false representation which the person knows or should know, will induce another to make a loan, intent to deceive may logically be inferred." *Id.* Here, we discern no reason for further extending the life of this litigation.

"Accordingly, the judgment of the district court is reversed and the cause is remanded for the entry of a judgment in favor of the Northern Trust Company.

Costs will be assessed against the defendant." (App. at 18).[6]

Garman contends that reversal without remand for a new trial was improper and deprived him of his right to present any evidence on the question of whether he intended to deceive the Northern Trust. (Petition at 3; 11). This contention puts out of view all the facts of the case, distorts the purposes underlying Rule 41(b) of the Federal Rules of Civil Procedure, and ignores the broad discretionary remand authority possessed by the federal courts of appeals.

A.

After carefully reviewing Garman's lengthy trial testimony regarding the reason why he failed to list approximately $50,000 in debts on the various financial statements he submitted to the Northern, the court of appeals was left "with the firm conviction that not only was Garman an evasive witness, but that his testimony was inherently incredible." (App. at 4). The validity of the court's characterization of Garman's conduct and his testimony is scarcely open to doubt. Indeed, a review of the testimony reveals that the court's characterization was, if anything, overly kind.

Testifying as an adverse witness at trial, Garman admitted that he owed the Northern $30,000 and that he had not recorded the approximately $50,000 in claims against him reflected on Schedule A-3 filed by Garman in the Bankruptcy Court.[7] That sworn Schedule is captioned

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[6] This disposition of the case was consistent with our prayer for relief in the court of appeals. (Brief For The Northern Trust Company at 43; Reply Brief For The Northern Trust Company at 17).

[7] The specific claims are set forth in the opinion at n.2 *See* App. at 2.

"Creditors Having Unsecured Claims Without Priority." (Northern's App. at 19).

Under examination at trial, both by his own counsel and by counsel for the Northern, Garman, "was a student of semantics", (App. at 5), sought to explain the reasons for these glaring omissions with the incredible contention that the Northern's form of Personal Financial Statement only called for the revelation of "debts or *liabilities*"[8] not of *"claims"* as required by Schedule A-3.[9]

The mendacity of this testimony is beyond dispute. Schedule A-3 states at the bottom "[t]hat none of the foregoing *indebtedness,* listed above are contingent, liquidated or disputed unless otherwise stated." And this Schedule also requires that the bankrupt list the "[n]ame of *creditor.*" and date the "claim was *incurred"* and "if evidenced by a *judgment.*" Surely, these words could not possibly convey to a "sophisticated businessman" (App. at 9) and a "student of semantics" that the information required on Schedule A-3 differed from that required by the Northern's form of personal financial statement. Garman's logomachy was clearly nothing more than a transparent evasion, and the court so found.[10]

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[8] *See* App. at 4-5.

[9] *See* Northern App. at 19. Garman testified that even though Schedule A-3 clearly reflected certain *"debts"* incurred between November, 1973 and February, 1975, he could not state what "debts" or "liabilities" were incurred by him in this period since the Schedule referred to "claims" while the questions asked spoke of *debts and liabilities.* The disingenuousness of this testimony was thoroughly explored by the court of appeals. *See* App. at 4-6.

[10] Garman's semantic punctiliousness at trial was of somewhat recent origin. During his deposition, Garman agreed with the characterization of the matters in Schedule A-3 as debts and obligations. The reliance on meaningless semantic distinctions exhibited by Garman is not, of course, without precedent. But where it has

(footnote continued)

Garman further testified that he advised individuals listed on Schedule A-3, all of whom were close friends, as to investments in the stock market.[11] For this advice, Garman was paid the fees shown as "counselling fees" on his financial statements. If there were gains, Garman was to share in the gains; in the event of losses, Garman would share in the losses. However, in the event that the stock became worthless, Garman, at trial, claimed he would not have any liability whatsoever. (App. at 6).

This testimony was wholly at odds with Garman's deposition testimony where, in laboring to explain why the "claims" on Schedule A-3 were omitted from his financial statements, Garman contended that he "would assume any losses at the rate of a hundred percent," (Record 15, at 8; 10-11; 13; 18) but that there was no "liability" unless and until the stocks went to zero. (Record 15, at 13; 18). Garman characterized these claims as "potential liabilities." (Record 13, at 119).[12]

(footnote continued)
occurred, it has been as resoundingly rejected by other courts as it was in this case. *See, e.g.,* Haimowich v. Mandel, 243 F. 338, 340 (3rd Cir. 1971) (bankrupt explained the falsity in his financial statement by saying that he thought he was asked to give only his "*accounts* payable" and not his "*bills* payable.") (Emphasis in original). Not surprisingly, the Third Circuit rejected this explanation.)

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[11] Garman admitted that there were no written agreements evidencing these arrangements.

[12] Contrary to some faint suggestion to the contrary (*see* Petition at 4, n.3 this deposition was used at the trial and was made, *without objection*, part of the Record on Appeal in the Seventh Circuit. Moreover, despite *extensive* references to and citation from the deposition in our brief on the merits in the court of appeals as well as in our brief in opposition to the request for a rehearing *en banc,* the petition uttered not a whisper of protest. Rather, it sought to overcome the devastating nature of this impeaching testimony by ignoring it.

It is obvious that the "student of semantics" came to realize that continued allegiance to his deposition testimony would render his obligations "contingent liabilities" and thus includable under that specific heading on the Northern's Personal Financial Statement. Hence, Garman at trial "changed positions as numbly as if dancing a quadrille," *Orloff* v. *Willoughby,* 345 U.S. 83, 87 (1953).

The decision of the court of appeals recognized that this was not a case in which an unsophisticated borrower was duped by an unscrupulous lender. Indeed, the record makes abundantly clear that, there were discussions between Garman and the Northern Trust at the time the various statements were submitted. Thus Mr. Bishop testified how, on December 9, 1970, when he approved the $5,000 loan to Garman, he examined in detail the written personal financial statement dated December 8, 1970, supplied by Garman. (Record 13, at 25-28). *Bishop told Garman the purpose of the statement and what the financial statement had to include.* (Record 13, at 72). Mr. Bishop also stated that when the Bank made the $4,000 loan to Garman, he relied upon Garman's written personal financial statement dated December 8, 1970. A day

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[13] Garman did admit that the $5000.00 claim of one Kenneth Stoen reflected on Schedule A-3 was incurred in 1978 and that this was a "liability" not shown on the financial statements he submitted to the Northern. (App. at 6). He sought to explain this omission on the ground it was offset by stock which *"I own for* Kenneth Stoen." (Record at 112) (Emphasis supplied). Apart from the fact that this explanation is not adequate, *Cf.,* Becker v. Seaboard Finance Co., 436 F.2d 778 (9th Cir. 1970); In Re Feldman, 86 F.2d 495 (7th Cir. 1936), this testimony is belied by ¶6 of the "Statement of Affairs For Bankrupt" in which Garman stated under oath that he did not hold property for anyone.

or two before that loan was granted, *Mr. Bishop had inquired of Garman if there had been any material change in his financial position since the date the December 8, 1970 financial statement was submitted to the Bank. Garman told Bishop there had been no change.* (Record 13, at 28-32). In addition, Bishop testified that he told Garman to submit to the Bank an undated and current financial statement, which Garman did the next day on December 22, 1971. *Id.*

Bishop further testified that on September 5, 1972, when he approved a $10,000 loan to Garman, he relied upon Garman's most recent written financial statement on file with the Bank, which was dated December 22, 1971. *On this occasion Bishop again inquired of Garman as to whether there had been any change in his financial condition, and Garman again told Bishop that there had been no change since he had given the Bank the December 22, 1971 financial statement.* (Record 13, at 32-33).[14]

On January 15, 1973, Mr. Bishop approved a $15,000 loan to Garman. In making the decision to loan Garman this amount, Mr. Bishop relied on Garman's personal financial statement dated December 22, 1971. *At the time of this loan, Garman once again informed Bishop that the financial statement of 12/22/71 was as complete and accurate a representation of his financial condition as it was when he had first presented that statement to the Bank.* In addition, Bishop testified that on this occasion he told Garman to give the bank a current financial statement, which Garman did on February 27, 1973. (Record 13, at 33-34; 63).

Despite the fact that Garman was examined in detail and without impediment by his own counsel at trial, he never contradicted any of Bishop's testimony!

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[14] These false statements are, of course, highly significant. *See* In Re West, 158 F.2d 858 (7th Cir. 1946); In Re Trimble, 55 F.2d 165, 166 (8th Cir. 1932).

B.

In light of this testimony, the Seventh Circuit manifestly was warranted in its finding that the testimony of Garman was "inherently incredible." And, in light of this testimony and the posture of the entire case, the court's disposition of the case was the only one that was "just under the circumstances." 28 U.S.C. §2106.[15]

> " 'If there be any one thing in the administration of law upon which the decisions, the texts, and the general opinion of bench and bar are in agreement, it is that evidence which is inherently unbelievable or incredible is in effect no evidence. * * * Courts are not required to believe that which . . . they judicially know to be incredible. . . .' " *Geighy Chemical Corp.* v. *Allen,* 224 F.2d 110, 114, n.5 (5th Cir. 1955).[16]

This principle is equally applicable to appellate review and disposition of cases under appropriate circumstances.

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[15] §2106 provides that:

"The Supreme Court or any other court of appellate jurisdiction may affirm, modify, vacate, set aside or reverse any judgment, decree, or order of a court lawfully brought before it for review, and may remand the cause and direct the entry of such appropriate judgment, decree, or order, or require such further proceedings to be had as may be just under the circumstances."

[16] *Accord* Quock Ting v. United States, 140 U.S. 417-420 (1891); Indiana Metal Products v. NLRB, 442 F.2d 46, 51 (7th Cir. 1971); Peters v. Fitzpatrick, 310 F.2d 704 (7th Cir. 1962); Urban Redevelopment Corp. v. CIR, 294 F.2d 328, 332 (4th Cir. 1961); Factor v. CIR, 281 F.2d 100 (9th Cir. 1960), *cert. denied,* 364 U.S. 933 (1962); Thomas E. Snyder & Sons v. Industrial Mollasses Corp., 270 F.2d 875 (7th Cir. 1959); Penn Texas Corp. v. Morse, 242 F.2d 243, 247 (7th Cir. 1957); Wong Ken Foon v. Brownell, 218 F.2d 444, 446 (9th Cir. 1955); Sun Life Assurance Co. of Canada v. Stacks, 187 F.2d 17, 20 (7th Cir. 1951); Albaugh v. Pennsylvania R.R. Co., 120 F.Supp. 70, 73 (D. D.C. 1954), *aff'd,* 219 F.2d 764 (D.C. Cir. 1955).

See e.g., Peters v. *Fitzpatrick,* 310 F.2d 704 (7th Cir. 1962); *Geigy Chemical Corp.* v. *Allen,* 224 F.2d 110, 114 (5th Cir. 1955). Thus, where, as here, evidentiary facts are not in dispute, a court of appeals can make its own findings without the necessity for remand for further proceedings. *See e.g., Magna Sales Co.* v. *Magna Alloys Research Pty.,* 545 F.2d 668, 671 (9th Cir. 1977); *Yunker* v. *CIR,* 256 F.2d 130, 133 (6th Cir. 1958); *Kostelac* v. *United States,* 247 F.2d 723, 726 (9th Cir. 1957).[17] The Seventh Circuit in *Smith* v. *Dravo Corp.,* 208 F.2d 388 (7th Cir. 1953), relying on 28 U.S.C. 2106, phrased the matter thusly:

> "Ordinarily, as to issues upon which no findings have been made, the court will reverse with directions to make findings and conclusions, but in equity, [18] where the record is complete or the evidence uncontradicted or entirely documentary, the appellate court is bound to decide the case so far as it is in condition to be decided, and direct such a decree as under all the circumstances may be proper." *Id.* at 391.

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[17] Since the bankruptcy judge made no finding of fact regarding Garman's intent, neither Rule 52(a) of the Federal Rules of Civil Procedure nor United States v. Zenith, 395 U.S. 100 (1969) have any relevancy. (*See* Petition at 9). Zenith's statement that Courts of Appeals should avoid deciding factual issues *de novo* was made with reference to appellate review of factual findings under Rule 52; it is manifestly irrelevant to the very different question of a Court of Appeals' scope of review and remand authority in the *absence* of an explicit finding. Equally inapplicable is the Petition's reference to James Burrough, Ltd. v. Sign of the Beefeater, Inc., 540 F.2d 266 (7th Cir. 1966) (Petition at 9). The most casual reading of page 273, *et seq.* of that opinion reveals why remand in that case was appropriate.

[18] Bankruptcy courts "are essentially courts of equity, and their proceedings inherently proceedings in equity. . . ." Continental Bank v. Rock Island R.R., 294 U.S. 648, 675 (1935). *Accord* Marin v. England, 385 U.S. 99, 103 (1966).

Finally, the disposition of this case by the Seventh Circuit accords with the course championed by Professor Moore:

> "On the other hand, it may not always be necessary for an appellate court upon reversal to direct a trial. For example, where the trial court grants defendant's motion to dismiss, but fails to enter Rule 52(a) findings as required by Rule 41(b), a remand may be required only for this limited purpose. In some instances, no further proceedings may be necessary other than the entry of judgment for the plaintiff. Where the facts are not disputed or where defendant has presented all his evidence upon being called as a witness for the plaintiff the appellate court upon reversal of a dismissal may properly direct the district court to enter judgment for the plaintiff." 5 J. Moore, Federal Practice, ¶41.13[2] at 41-185 (2d Ed. 1980) (footnotes omitted).

No one even remotely familiar with the singular history of this litigation, *see supra* at n.2, and the irrefragible proof of Garman's criminality fairly could suggest that the court of appeals erred in "discern[ing] no reason for further extending the life of this litigation." (App. at 18). Rather, this is one of those cases presenting "circumstances in which a federal appellate court is justified in resolving an issue not passed on below, as where the proper resolution is beyond any doubt . . . or where 'injustice might otherwise result.'" *Singleton* v. *Wulff*, 428 U.S. 106, 121 (1976). *Cf., Haynes* v. *United States*, 390 U.S. 85, 100-01 (1968). *See also Kosty* v. *Lewis*, 319 F.2d 744, 749 (D.C. Cir. 1963).

The cases cited at pages 9 through 11 of the Petition are not to the contrary. They merely enunciate the general proposition that a reversal of a judgment improperly dismissing a complaint at the close of a plaintiff's case-in-chief must be remanded for trial in order that the defen-

dant can present his case. However, since "general propositions do not decide concrete cases," *Lochner* v. *New York,* 198 U.S. 45, 74 (1905) (Holmes, J., dissenting), there must be a more critical analysis of those authorities and their applicability here than the petitioner has been willing to undertake.

In each of the cases cited in the Petition, absent a remand, the defendant would have been deprived of the opportunity to present any evidence in opposition to that offered by the plaintiff and thus would have been deprived of his "day in court." A review of the record demonstrates that no comparable situation exists here.

In none of the cases cited in the Petition did the defendant offer any evidence or did he testify regarding the crucial elements not only of the plaintiff's case but his own defense as well.[19] Here, Garman was called as an adverse witness by the Northern. During his "direct" examination, he admitted that the various financial statements he submitted to the Northern between 1970 and 1973 failed to include some $50,000 in debts and claims which were listed on the sworn schedules filed in the Bankruptcy

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[19] With all deference, we fail to perceive the reason for the petition's reliance on Riegel Fiber Corp. v. Anderson Gin Co., 512 F.2d 784 (5th Cir. 1975). Riegel Fiber Corp. most surely does not support the proposition that "where one of the defendants testify [sic] as an adverse witness, the defendants still have a right to offer their evidence should the dismissal order be reversed." (Petition at 9). The only question presented in that case was the extent of the evidence the *plaintiff* would be allowed to present following a reversal of an improperly granted Rule 41(b) dismissal entered in favor of the defendant. The Fifth Circuit's opinion did not pretend to deal with the very different questions presented in this case. Properly read, the Fifth Circuit's decision in *Riegel Fiber Corp.* is not contrary to its decision in *Geighy Chemical Corp.* v. *Allen,* discussed *supra* at 12.

Court. During his "direct" examination and later during the unobstructed examination by his own counsel, Garman testified regarding his intent in providing these statements to the Northern and the reasons for the omissions in the statements. It was this explanation which the court of appeals found to be inherently incredible as a matter of law.

C.

It has been rightly said that "[i]n a court of conscience deliberate concealment is equivalent to deliberate falsehood." *Crosby* v. *Buchanan,* 90 U.S. (23 Wall.) 420, 454 (1875). Measured against this standard, the presentation of the petitioner does not fare too well. Indeed, in certain respects, the Petition is as disingenuous as was the trial testimony itself. For example, the Petition states that as a result of the dismissal of the Northern's complaint at the close of its case, Garman never presented "any of its [sic] own evidence," even though there were some twenty exhibits which Garman would have used had he had the opportunity. (Petition at 3, n.2; 11).

There are two essential difficulties with this tantalizing statement. First, neither in this Court nor in his presentation to the court of appeals has there ever been the slightest attempt to explicate the nature of this mysterious "evidence." Instead, there is only Garman's insidious *ipse dixit* that, despite the five and one half year pendency of this case, he has been deprived of his "day in court."

Second, and more importantly, the contention ignores the events which transpired at trial. However, "[u]nless we are to reach judgments as did Plato's men who were chained in a cave so that they saw nothing but shadows, we should consider the facts of this case at least as a hypothesis to test the validity of the conclusions. . . ."

Douglas v. *City of Jeanette,* 319 U.S. 157, 166 (1942) (Jackson, J., dissenting).

Of the twenty defense exhibits, half were documents dated between January, 1962 and 1968. (App. at 21-22). The balance bore dates between 1970 and 1973. (*Id.*) The bulk of these documents consisted merely of credit advices, the actual demand notes, out-of-date financial statements, promissory notes, letters to Garman demanding payment, and letters from Garman declining to pay. *Id.* Quite apart from the manifest irrelevancy of these exhibits to the critical questions in the case, Garman's attorney used these exhibits extensively, and without restriction, during his cross examination of the Northern's witnesses (*see* App. at 22-44). It is thus rather illegitimate to suggest that the action of the court of appeals prevented Garman from having that full and fair hearing that the Fifth Amendment requires. (Petition at 3; 11).

Given the inherently incredible nature of this testimony and the indisputable nature of the balance of the Northern's case, the court of appeals refused to further prolong, unnecessarily, the litigation. In essence, the Panel correctly perceived that only by "modifying his version of the facts" on remand could Garman hope to prevail. *See Fisher* v. *Volz,* 496 F.2d 333, 349, n.2 (3d Cir. 1974). This, neither the imperative of judicial integrity[20] nor the salutary purposes underlying 28 U.S.C. §2106 will allow. *See Fisher* v. *Volz, supra. Compare Morgan Guaranty Trust Co. of New York* v. *Martin,* 466 F.2d 593, 600 (7th Cir. 1972).

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[20] *Compare* Harris v. New York, 401 U.S. 222 (1971); Walder v. United States, 347 U.S. 62 (1954); J. Cole, Impeachment With Unconstitutionally Obtained Evidence: Coming To Grips With The Perjurous Defendant, 62 Nw. J. C. L. & CRIM. 1 (1971).

CONCLUSION

Rule 17 of the Rules of this Court provides that "[a] review on writ of certiorari is not a matter of right, but of judicial discretion, and will be granted only when there are special and important reasons therefor." Among the reasons which will justify granting of the writ is the issuance of a decision by a federal court of appeals which is in conflict with decisions of other circuits on the same subject or which "has so far departed from the accepted and usual course of judicial proceedings . . . as to call for and exercise of this Court's power of supervision." Only literary perversity or jaundiced partisanship could suggest that either of these criteria for review has been met in the instant case.

Wherefore, for the foregoing reasons, The Northern Trust Company respectfully requests that the Petition For A Writ of Certiorari be denied.

Respectfully submitted,

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APPENDIX

APPENDIX

In the

United States Court of Appeals

For the Seventh Circuit

No. 79-1631

IN THE MATTER OF: BEN GARMAN, Bankrupt.
THE NORTHERN TRUST COMPANY,

Plaintiff-Appellant,

v.

BEN F. GARMAN,

Defendant-Appellee

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 75 B 1111

HUBERT L. WILL, *Judge.*

Argued February 19, 1980—Decided April 29, 1980

Before CASTLE, *Senior Circuit Judge,* PELL and TONE, *Circuit Judges.*

PELL, *Circuit Judge.* Section 17(a)(2) of the Bankruptcy Act of 1938, 11 U.S.C. § 35(a)(2), provides that an individual's debt shall not be discharged in bankruptcy if that debt or its renewal is the result of money obtained "in reliance [by the creditor] upon a materially false statement in writing respecting [the debtor's] financial

condition made or published . . . with intent to deceive. . . ." This appeal calls upon us to decide, *inter alia*, whether non-dischargeability is appropriate only where the creditor's reliance under § 17(a)(2) is "reasonable."

Ben F. Garman, the bankrupt, a life insurance salesman, had been a customer of the Northern Trust Bank (Northern) in Chicago since 1962. Between December, 1970, and March, 1973, Garman borrowed various sums from the Northern resulting in a total indebtedness on November 1, 1973, of $30,000. On that date, Garman executed a renewal note to the Northern for the entire outstanding amount.

There is direct and unimpeached testimony in the record that the Northern, at least in part, expressly relied upon three financial statements submitted by Garman in making these loans.[1] It is uncontested by Garman that these statements omitted listing approximately $50,000 in "claims" that Garman later listed in his petition for bankruptcy.[2] These claims, however, are recorded as hav-

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[1] There is no requirement that the creditor place exclusive reliance on the financial statement. Partial reliance is sufficient. *See Carini* v. *Matera*, 592 F.2d 378 (7th Cir. 1979); *Cunningham* v. *Elco Distributors*, 189 F.2d 87 (6th Cir. 1951).

[2] Garman's transactions with the Northern can be summarized in the following schedule:

	Date	Amount	Date of statement relied upon	Amount of claims omitted
1.	12/ 9/70	$5,000 (loan)	12/ 8/70	$49,800
2.	12/21/71	$4,000 (loan)	12/ 8/70	$49,800
3.	9 /5/72	$7,500 (loan) $2,500 (renewal)	12/22/71	$51,170
4.	1/15/73	$15,000 loan)	12/22/71	$51,170
5.	3/ 2/73	$5,000 (loan)	2/27/73	$51,170
6.	11/ 1/73	$30,000 (renewal)	2/27/73	$51,170

ing arisen prior to the time Garman filed the statements with the Northern. Had these amounts been included as potential liabilities in the statements, they would have substantially reduced Garman's net worth, in some instances to less than zero.

Upon Garman's failure to pay the $30,000 when due in April of 1974, the Northern filed suit against him for this amount in state court. On February 6, 1975, prior to judgment in the state court, Garman filed a voluntary petition in bankruptcy listing as unsecured claims to be discharged the $30,000 debt to the Northern as well as the $50,000 in claims not listed on his financial statements. The Northern filed a complaint to prevent the discharge of the $30,000 debt pursuant to § 17(a)(2), and a hearing was held on the issue before a bankruptcy judge on March 28 and 29, 1977. At the hearing, the Northern introduced the testimony of Charles S. Bishop, a Northern vice-president, who had approved most of the loans to Garman, and Carol King, a loan officer who had approved the November 1, 1973 renewal, regarding their reliance on the Garman statements.[3] The Northern also introduced the various notes and statements signed by Garman. Each financial statement provided that it was "a true and complete statement of my financial condition, and details relating thereto. . . . I agree that if any material change occurs I will immediately notify you, unless you are so notified you may continue to rely upon the statement hereon given." Bishop

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[3] Although King, unlike Bishop, did not specifically state that she had "relied" upon Garman's filed statements when approving the renewal, she did state she had "reviewed" the statements and Garman's credit file as a whole prior to granting her approval. Her reliance on the statements, which at the very least was a partial basis of her decisions, is implicit in her testimony.

testified that had he known of the $50,000 in claims omitted from the statements, he would not have made the loans.

Garman, testifying as an adverse witness, conceded that he had failed to list the $50,000 in claims on the financial statement, but maintained that the omission did not render the statements false. Our examination of his testimony leaves us with the firm conviction that not only was Garman an evasive witness, but that his testimony was inherently incredible. A few illustrations are sufficient to demonstrate our conclusion. One of the creditors listed on Schedule A-3 of the bankruptcy petition was a Dr. Solomon with the claim stated as being approximately $10,800. Garman's attention was directed to the statement at the bottom of the page of Schedule A-3 that "none of the foregoing indebtedness, listed above, are contingent, liquidated or disputed, unless otherwise stated." When asked about the debt to Solomon which had been listed in the schedule without qualification, Garman responded, "[Y]ou keep referring to a debt. We are talking about unsecured claims. I am not talking about any debt." This was followed by an assertion that when he "signed that statement [he] did not acknowledge that was a debt." The record does not indicate whether he was referring here to the bankruptcy schedule or to the financial statement. Either interpretation, however, would fail of verity. If he was referring to the schedule, it clearly refers to "indebtedness." On the other hand, if he was referring to the financial statements, which were signed in the early 1970's, the Solomon claim was not listed although on the schedule he listed it as having been incurred in October, 1968. When asked specifically about listing this item on the financial statements, he said, "It talks about contingent liabilities, sir. I did not have a contingent liability at that time." When the Solomon matter was pursued further, this non-illuminating colloquy followed:

Q. I will rephrase the question.

Mr. Garman, in examining the financial statements marked as Plaintiff's Exhibit Nos. 2, 4, and 7, could you tell me if, reflected on any one of those financial statements, is this claim of Dr. Solomon that is reflected on any one of those three financial statements?

A. I'm sorry, I can't answer the question.

I find the discrepancy between claim and liability. This is talking about a liability and this is talking about a claim.

Q. You are not answering my question.

A. I can't answer your question.

THE COURT: That is an answer.

The statement that he could not answer the question was repeated with regard to another item of indebtedness listed on the bankruptcy schedule as having been incurred in February, 1972, even though he was being shown a subsequent-in-time financial statement which clearly did not include the debt. On subsequent references to the financial statements, Garman admitted that items were not listed there but did appear on the bankruptcy schedule, including a $4,000 indebtedness to another bank resulting from the various loans extended over the past five years, and a promissory note to an estate for $5,000 which related back to January, 1968.

Professing that he was "a student of semantics," Garman periodically stated that he could not answer questions, stating on one occasion, "[Y]ou ask me about debts, on the other hand, you are talking about claims." When examined by his own counsel, Garman, in significant candor, related that it had been made clear to him when he was filing in bankruptcy that possible claims should be listed because once he had filed he could not go back and claim that he had forgotten them. His concern about not having possible claims discharged in bankruptcy did not extend

to an equal disclosure when he was borrowing money from Northern. Garman further testified that the unlisted items on the financial statements were not legal documents, they were just informal agreements, and that he did not feel that the word "debt" did "justice to what was involved here as the listing of a claim." The gist of his testimony with regard to a substantial amount of the unlisted items was that Garman would purchase, or would recommend purchase, of certain investments which would be bought with money from friends, and he would share in 50% of the gains but would be responsible for 100% of the losses. He testified he did not consider these as "debts" although he did concede that the $5,000 promissory note, which was also unlisted on the financial statements, was an exception. In sum, while he considered that he had to list all possible claims on the bankruptcy schedule, he felt no similar compulsion on the financial statements even though an answer was required on "other contingent liabilities." As early as 1970, however, he was aware of this part of the statement because he listed a contingent liability of $37,000 as an endorser on notes. Subsequent statements listed no contingent liabilities.

At the conclusion of the hearing, the bankruptcy judge issued no written findings and made no oral findings regarding the materiality of the omissions in the statements or Garman's intent when he filed the statements. Rather, the bankruptcy judge held that the Northern had failed to establish its entitlement to nondischarge of Garman's debt to it because it had not proved it had "reasonably relied" upon the statements. Although the bankruptcy judge's statements do not make clear whether he was basing his decision on a finding of no actual reliance or of no reasonable reliance, the district court on appeal held, correctly we believe, that "it is clear that the bankruptcy

judge's dismissal was predicated upon his findings of no reasonable reliance.'"[4] The district judge then affirmed the bankruptcy court stating: "In addition to the requirement that the creditor actually relied, it is clear that § 35 (a)(2) requires that the creditor's reliance must have been reasonable." Viewing what it held to be a finding of fact by the bankruptcy judge, the district court held that the finding that the Northern could not have reasonably relied upon these statements was not "clearly erroneous."

Initially, we note that § 17(a)(2), unlike its successor,[5] does not by its terms require a showing of "reasonable reliance" and requires only a showing of reliance in fact.[6] Nevertheless, Garman relies upon a number of decisions ostensibly requiring a showing of reasonableness. *Carini* v. *Matera,* 592 F.2d 378 (7th Cir. 1979); *Kentile Floors, Inc.* v. *Winham,* 440 F.2d 1128 (9th Cir. 1971); *In re: Smith,* 424 F.Supp. 858 (M.D. La. 1976); *In re: Adams,* 368 F.Supp. 80 (D.S.D. 1973); *Sweet* v. *Ritter Finance Co.,*

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[4] As noted above, Bishop's testimony that he actually relied on the statement in making the loans was direct and unimpeached, and the bankruptcy judge stated "there is no reason to doubt anything that Mr. Bishop stated in answer to the questions in my opinion.

[5] Section 523(a)(2)(B) of the Bankruptcy Act of 1978 provides, in relevant part:

> A discharge under . . . this title does not discharge an individual debtor from any debt—for obtaining money . . . or an extension [or] renewal, by—use of a statement in writing—(i) that is materially false; (ii) respecting the debtor's . . . financial condition; (iii) on which the creditor to whom the debtor is liable for obtaining such money . . . or credit *reasonably* relied; and (iv) that the debtor caused to be made or published with intent to deceive. . . . (Emphasis added.)

[6] Whether the new § 523 will be subject to the same interpretation we apply today to § 17(a)(2) is a question that will have to await another day for resolution.

263 F.Supp. 540 (W.D. Va. 1967); *In re: Disbrow,* 20 Colliers Bankr. Cases, 1149 (D. Ver. 1979); *In re: Ducote,* 4 Bankr. Ct. Dec. 943 (W.D. La. 1978); *In re: Gibbs,* 9 Colliers Bankr. Cases, 608 (M.D. Fla. 1976); *In re: Arden,* 2 Bankr. Ct. Dec. 204 (D.R.I. 1975); *Cash Finance Service, Inc.* v. *Haisch,* 173 So.2d 851 (La. Ct. App. 1965). We believe, however, Garman misinterprets these cases in arguing that they bar the Northern's requested relief.

Although some of the mentioned cases do, in fact, refer to "reasonable" or justifiable reliance as a requirement under § 17(a)(2), they do not require the court, as was done in the present case, to undertake a subjective evaluation and judgment of a creditor's lending policy and practices. These cases simply stand for the proposition that reasonableness is circumstantial evidence of actual reliance; that is, dischargeability shall not be denied where a creditor's claimed "reliance" on a "financial statement" would be *so* unreasonable as not to be actual reliance at all. The opinions relied upon either state this directly, *e.g., Smith, and see Adams* and *Sweet,* or the lack of actual reliance was implicit in the record. In *Arden,* for example, the court held that the creditor knew the alleged misrepresentation was false at the time the loan was made and therefore could not have "reasonably" relied on the "misrepresentation." The court's decision to allow discharge, furthermore, was based upon its holding that the creditor had failed to prove the debtor's intent to defraud. In *Sweet,* one debtor, the husband, could neither read nor write except to sign his name on the statement filled out and signed by his wife. The entire transaction was completed in "no more than two minutes" and the creditor, although charging 30% interest on a portion of the amounts lent, never asked any questions concerning the listed assets or liabilities. The court noted the creditor

was simply "taking advantage of a borrower's ignorance" and held that indications that the creditor was well aware of the unsound financial condition of the debtor yet exercised an "almost studied disregard for the truth . . . is enough in most instances to preclude a later claim by the loan company that is reliance on the false financial statement was reasonable." 263 F.Supp. at 542. In *Kentile Floors,* and *Disbrow,* as in *Sweet,* the creditor possessed information that conflicted with the apparent financial well-being portrayed on the debtor's financial statement. In *Cash Finance,* the statement was all but illegible and the court found that it was "obvious" that the list of debts in the statement was incomplete. In *Ducote,* the money was transferred to the debtor at the same time the first financial statement was submitted, thus indicating that "the loan had already been approved when [the debtor] filed the signed financial statement." 4 Bankr. Ct. Dec. at 944. *See also Gibbs and Sweet, supra.* In *Smith* and *Gibbs,* the debtor was a total stranger to the lender and the "financial statement," which was "nothing more than a typewritten statement on the stationery of the company whose financial status they purported to represent," *id.* at 862, was unsigned by the debtor. In *Carini,* this court simply stated, "And, of course, such reliance must be reasonable" while affirming the district court's finding of reasonable reliance. 592 F.2d at 381.

These cases present factual circumstances far different from the one before us here. Garman, the debtor, was a sophisticated businessman who had a long-standing and apparently successful business relationship with the Northern for many years prior to his default. *See, Carini,* at 381. The financial statements he signed did not on their faces indicate the presence of any material misrepresentations or omissions, showed his net worth well in excess

of the loaned amount, and affirmatively required him to notify the Northern in the event of any material change in his financial condition. *Compare, Disbrow.* Furthermore, the Northern had no information indicating that anything stated in the financial statements might be materially false.[7] In sum, there are no facts presented suggesting that the Northern utilized the financial statement simply as a "perfunctory device to be used to contest discharge, and not used to be relied thereon," 1A Colliers on Bankruptcy. ¶ 17.16 at 1636 n.17 (14th ed., 1979), was simply "burying its commercial head in the sand," *Arden, supra,* at 207, or that the Northern's reliance on the financial statements was so unreasonable as not to be actual reliance at all.

Garman protests, however, that to allow Northern to bar discharge in this case would defeat the well-established principle that the Bankruptcy Act "ultimately favors the debtor who invokes its protection." *In re: Schmelzer,* 350 F.Supp. 429, 435 (S.D. Ohio 1972), *aff'd,* 480 F.2d 1074 (6th Cir. 1973). This would be true, of course, in every case where discharge is denied, yet this has failed to preclude the denial of discharge in cases where § 17(a)(2) applied. We believe the Act was meant to discharge only the *honest* debtor from his debts, *Williams* v. *United States*

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[7] Although it is true Garman was in default on at least one of the loans at the time of the November 1, 1973 renewal, this does not necessarily indicate that the financial statement misrepresented his financial condition. This fact might well indicate that it was a poor business decision to grant the renewal at that time in that Garman apparently would be required to sell assets to repay his debt. *See* discussion in text, *infra.* However, whether or not it was a poor business decision is not the proper inquiry. Rather, the proper inquiry is whether the claimed reliance on the financial statement accurately to portray Garman's net worth in excess of the debt was so unreasonable as not to be reliance in fact.

Fidelity & Guaranty Co., 236 U.S. 549, 555 (1915), and that the Act should be liberally applied to protect the bankrupt only in those cases where there is no intent to violate its provisions. *In re: Schwartz*, 133 F.2d 216, 217 (7th Cir. 1943); *Cunningham* v. *Elco Distributors*, 189 F.2d 87, 89 (6th Cir. 1951). As was stated by the Supreme Court in *Bruning* v. *United States*, 376 U.S. 358, 361 (1964):

> . . . petitioner [is not] aided by the now familiar principle that one main purpose of the Bankruptcy Act is to let the honest debtor begin his financial life anew. As the Court of Appeals noted, § 17 is not a compassionate section for debtors. Rather, it demonstrates congressional judgment that certain problems . . . override the value of giving debtors a wholly fresh start. (Footnote omitted.)

See also United States v. *Sotelo*, 436 U.S. 268, 278-79 (1977).

The bankruptcy and district judges' analyses of the present case, in fact, illustrate the very problems potentially arising from their interpretation of the above mentioned cases. Indeed, their analyses did not address whether the Northern's reliance *on the statements* was reasonable. Rather, they expressed their judgment on whether the decision *to loan Garman the money* was reasonable.[8] They did not hold that the financial statements

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[8] An excerpt from the transcript of the bankruptcy hearing is indicative:

> The Court: The way I look at reliance if you rely on a piece of paper then it has to be that you are able to make a proper business decision.
>
> * * *
>
> What if I think the person who relied on [the statement] is a complete fool?
>
> * * *

(footnote continued)

showing Garman's net worth in excess of the loaned amount was inherently unreliable; rather, they were concerned by the fact that the Northern would have based its decision to lend money on the net worth and nature of the assets of the debtor rather than the debtor's income.[9] However, it is not the court's duty under § 17(a)(2) to

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(footnote continued)

Mr. Webb (Northern's counsel): . . . Therefore, there is no question that the financial statement was relied upon. Now whether or not she should have relied upon it is the question your honor is asking?

The Court: Yes . . . I say that is *bad judgment.*

* * *

Mr. Webb: But the bank did rely upon it.

The Court: Then I fault their judgment. I fault their reliance . . . and I think that is bad judgment if they relied upon this, even partially relied upon this.

* * *

The Court: The statement dated 2/27/73 does not justify the renewal or extension of credit to Mr. Garman of $30,000. . . . *It is just bad business conduct.*

* * *

The Court: I find it difficult to impose on Mr. Garman the responsibility of the bank's actions in making these loans where I believe that the various statements supposedly relied upon [by] the bank do not warrant in the court's opinion the extension of the credit. . . . (Emphasis added.)

[9] At one point the bankruptcy judge stated:

Then I look to the financial statement and I say how can anyone look at this personal financial statement . . . which is the one dated February 27, and say on April 30, 1974 [the due date of the renewal note] Ben F. Garman will be able to pay $30,000.

* * *

(footnote continued)

second guess a creditor's decision to make a loan or to set loan policy for the creditor. If a lender chooses to let net worth rather than income be the determinative factor in loan decisions, it is not for the court to say that this is bad business policy requiring discharge of the resulting debt in bankruptcy. The present issue for the court is simply whether the bankrupt obtained credit, or a renewal, through the creditor's reliance on a materially false financial statement containing information apparently sufficient to obtain an accurate picture of the debtor's financial condition with regard to a reasonable decisional factor in the loan decision, filed by the debtor with the intent to deceive the creditor. The creditor need establish only its reliance in fact, although its claims to reliance cannot be so unreasonable as to defeat a finding of reliance in fact. Given this reliance, the court, with the benefit of hindsight, should not base its decision regarding discharge on whether *it* would have extended the loan. In the present case, the Northern's financial statement form requested sufficient information to obtain an accurate picture of the debtor's net worth, a reasonable decisional factor in the loan decision. To say the Northern should have looked to Garman's income flow instead of net worth is irrelevant to the § 17(a)(2) issues.

(footnote continued)

> Where is he going to get that money? He has $80,000 in—he is not going to sell his house. His cash in the bank, what is he going to do with that? He will keep that. He has life insurance cash value. Okay. On the back of it he says he has a loan of $5,000. Will he get another loan? All right, there is $5,000. He has a car. Is he going to sell his car? His coin collection. Are we going to ask him to sell his coin collection? He probably will not.
>
> A lot, $20,000. I do not know what that lot is, whether it is a new home or an old home.

The bankruptcy and district judges were also concerned, however, with the fact that at the time the final renewal was granted on November 1, 1973, the most recent financial statement was more than seven months old. We also note that prior loans were granted in reliance upon financial statements that were slightly more than a year old. Although this fact also may raise questions regarding the business judgment shown in the decision to lend the money, we do not think this time lapse renders Northern's reliance on the statements so unreasonable as not to be reliance in fact. In *Gerdes* v. *Lustgarden,* 266 U.S. 321 (1924), the debtor submitted a financial statement on January 5, 1920, containing, as in the present case, a statement that he would notify the creditor as to any material changes in his financial condition, and that the creditor could continue to rely upon the statement until so notified. Based upon this representation, the creditor, a bank, advanced funds in October and November 1920 and in February of 1921. Upon the debtor's bankruptcy, the bank moved to avoid discharge of the debt pursuant to § 14(b) of the Bankruptcy Act of 1910. The bankruptcy referee allowed the discharge holding that even if the bank had in fact relied upon the statement, "it had no right to so do, since in view of the financial depression prevailing in 1920, the 'reasonable time' for which the statement remained a 'continuing statement' had expired when the credits were extended." 266 U.S. at 324. The district court reversed, finding that the bank had a right to rely upon the statements, but the court of appeals reversed the district court judgment, holding that the lapse of time rendered the bank's reliance unjustified. The Supreme Court reversed the court of appeals, however, stating:

> The only essentials to the statutory bar . . . are (a) that the written statement was made for the purpose of obtaining credit; (b) that it was materially false;

> and (c) that credit was obtained upon it. If these are established, the vice inherent in the original falsity of the statement is not remedied by the lapse of time; and if the creditor extends credit upon such a false statement while it is still in force and binding upon the bankrupt, within the time in which he intended it should serve that end, it does not lie in his mouth to say that by reason of extrinsic circumstances the creditor was unjustified in relying upon it. In short, the lapse of time is only material in determining whether credit was extended within the period intended, while the statement was still binding on the bankrupt, and whether the creditor in fact extended credit upon the faith of the statement.

266 U.S. at 326.

We hold that the same conclusion is appropriate in the present case. Garman clearly filed the financial statements for the purpose of obtaining credit. The financial statements were materially false when they were filed. Finally, the creditor extended credit upon the faith of the statements.

The district and bankruptcy judges were also concerned, however, with the fact that the Northern took no steps to confirm or verify the information Garman set forth in his financial statements. They found, therefore, that any reliance the Northern placed in these statements was unreasonable. In *Carini, supra,* this court faced a similar contention and rejected it, as we do here. *Carini* involved a creditor who had the opportunity to verify the representations of the debtor's solvency made by the debtor in a written statement, and by the debtor's accountant orally. The creditor declined the opportunity "because he and [the debtor] were like brothers, and even had he seen [the verification], he would not have been able to understand [it]." *In re: Matera,* 436 F.Supp. 947, 949 (E.D.

Wis. 1977). Nevertheless, this court affirmed the bankruptcy and district judges' refusal to discharge the debt, stating: "Taking into account . . . the close friendship between the parties, . . . the repetition of the false representations over a six-month span, and the other circumstances prior to the loan, the finding of reasonable reliance is supported by the evidence." 592 F.2d at 381. In the present case, we hold that the failure of the Northern to verify the information contained in Garman's statements was not so unreasonable as to justify a finding that there was no actual reliance. Garman was a longtime customer of the bank and repeated his alleged misrepresentations over a three-year period. The statements themselves contain no information indicating that further investigation may be required, nor is there any allegation that further investigation would have uncovered the great majority of unlisted claims that were attributable to informal and oral arrangements between Garman and his friends. Furthermore, although a creditor is not entitled to rely upon an obviously false representation of the debtor, this does not require him or her to view each representation with incredibility requiring verification. "The law recognizes a duty of each to refrain from even attempted deceit of another with whom he deals and the right of the latter to assume he will do so. . . ." *Jacobsen* v. *Whitley,* 138 Wis. 434, 120 N.W. 285, 286 (1909). Absent any facts reasonably indicating verification was necessary, we are not persuaded that the Northern's failure to verify rendered its reliance so unreasonable as to discharge Garman's debt.

One further point deserves mention. On appeal, the district court affirmed, *inter alia,* the bankruptcy judge's determination that because the November 1, 1973 renewal note extinguished all prior notes signed by Garman, the only circumstances to be evaluated under § 17(a)(2) were

the circumstances surrounding that last renewal. To adopt such a position, however, is to hold that because the Northern failed to discover Garman's misrepresentation at the time of the renewal, all prior alleged misrepresentations by Garman were excused. This we refuse to do. Although the renewal note did, in fact, result in the repayment of the prior notes for bookkeeping purposes, it is clear that in actuality the "renewal" was exactly what its name implies, an extension of the time in which Garman was required to repay the pre-existing debt. Garman's counsel acknowledged this when he conceded at the oral argument that the $30,000 renewal and the prior notes were all part of the same loan transaction.

Similarly, the fact that the November 1, 1973, renewal was initiated by the Northern rather than Garman is irrelevant to the instant issue. The fact remains that Garman signed financial statements stating that they could be relied upon until he informed the Northern otherwise. He cannot avoid liability on these statements simply because the Northern found that renewing the debt rather than immediately seeking its judicial remedies was in its interest. The Northern properly pleaded and appealed its contentions regarding the whole of Garman's outstanding debt, and the district court, therefore, improperly limited its review to only those circumstances surrounding the November 1, 1973 renewal.

Having held that the bankruptcy and district judges applied an improperly stringent legal standard in this case in finding that the Northern's reliance was "unreasonable," and therefore did not justify a bar to discharge, we see no reason to rule upon whether the bankruptcy judge's finding that Northern failed to meet the more stringent standard was to be reviewed under the "clearly erroneous" or some other standard. Our determination turns simply on a question of law.

Having thus determined that a reversal is necessary, our only remaining question concerns what course further judicial attention to this case should take. We have already set forth that the elements adverted to in *Gerdes* exist without dispute in the record of this case. The remaining question is the matter of "intent to deceive." We find guidance in *Carini, supra,* 592 F.2d at 30:

> In addition, the courts require a showing of fraudulent intent or moral turpitude on the part of the debtor, i.e., an intent to deceive. . . . These questions of knowing or reckless falsehood and intent to deceive are questions of fact, . . . and the bankruptcy court's findings on those issues are conclusive unless clearly erroneous. . . . (Citations omitted.)

Here, of course, we are not aided by a finding on this question of fact. Nevertheless, in view of the inherent incredibility of Garman's testimony, which we have previously noted, the continuing omissions in the context of the representations of completeness in the financial statements, in the words of *Carini, supra* at 380, "were grossly reckless at a minimum. . . . Indeed, where, as here, a person knowingly or recklessly makes a false representation which the person knows or should know, will induce another to make a loan, intent to deceive may logically be inferred." *Id.* Here, we discern no reason for further extending the life of this litigation.

Accordingly, the judgment of the district court is reversed and the cause is remanded for the entry of a judgment in favor of the Northern Trust Company. Costs will be assessed against the defendant.

A true Copy:
Teste:

.....

Clerk of the United States Court of Appeals for the Seventh Circuit

The Court: Which exhibits are you going to—

Mr. Webb: I will state for the record, your Honor, the exhibits which I intend to use which there is a stipulation as to foundation are: Plaintiff Exhibit Nos. 1, 3, 5, 6, 8, and 9; those are all promissory notes of Northern Trust Company signed by Mr. Garman.

In addition, Plaintiff Exhibit No. 2, Plaintiff Exhibit No. 4, and Plaintiff Exhibit No. 7 are personal financial statements of Mr. Garman filed with the Northern Trust Company.

The only other exhibit I anticipate using, your Honor, is an exhibit I have marked Plaintiff—10 which is, in effect, part of these proceedings. It is a bankruptcy petition which I anticipate using, but the document itself is part of the record before the Court at this time.

The Court: Thank you.

And, as I understand it, Mr. Crane, you stipulate as to the foundation of these various exhibits?

Mr. Crane: Yes, I do.

The Court: What exhibits do you wish to use?

Mr. Crane: Your Honor, the defendant wishes, I think I will have to enumerate them one by one because they are kind of lengthy.

As its Group Exhibit No. 1, all of these documents are copies of documents in the bank's loan or credit file which I got from the plaintiff pursuant to motion to produce, the Defendant's Group Exhibit No. 1 which consists of an interoffice memorandum dated January 12, 1962; a loan memorandum dated January 12, 1962; a letter from the Northern Trust, dated January 15, 1962, to Mr. Hugh Fanning; and an undated memo signed GSS which Mr. Webb would agree appears to be part of that same dated transaction.

Mr. Webb: That is correct.

Mr. Crane: As Defendant's Exhibit No. 2, an interoffice memorandum from the Northern Trust, dated November 27, 1963.

As Defendant's Exhibit No. 3, an interoffice memorandum dated January 21, 1964.

As Defendant's Exhibit No. 4, consisting of two documents, I'm sorry, one document with two notations, a note from Ben Garman, the bankrupt, dated 7/3/64; and a handwritten response, dated 7/8/63, I think there is an error in the date, to that by the bank.

Is that correct, Mr. Webb?

Mr. Webb: Yes, that is correct.

Mr. Crane: As Defendant's Exhibit No. 5, an interoffice memorandum, dated June 15, 1967, and a loan memorandum dated, June 14, 1967.

As Defendant's Exhibit No. 6, a personal financial statement, dated January 5, 1962.

The Court: These all go in chronological order?

Mr. Crane: No, I'm sorry, your Honor, they go back at the moment.

The Court: Is that January 5, 1962?

Mr. Crane: Yes, sir.

As No. 7, a financial statement, dated October 22, 1964.

As No. 8, a financial statement, dated May 18, 1966.

No. 9, a financial statement, dated June 22, 1967.

No. 10, a financial statement, dated December 9, 1968.

Defendant's Group Exhibit No. 11, which consists of 5 documents, an interoffice memorandum, dated December 9, 1970, which bears on it a notation on it dated, September 3, 1971, it is apparently two documents in one; a loan memorandum, dated December 9, 1970; a personal financial statement, dated December 8, 1970; and a credit advice, dated December 9, 1970.

As Defendant's Exhibit No. 12, a loan memorandum dated June 17, 1971.

Defendant's Exhibit No. 13, consisting of 3 documents, a loan memorandum, dated December 21, 1971; a credit

advice, dated December 21, 1971; and a personal financial statement, dated December 22, 1971.

Defendant's Exhibit No. 14, a loan memorandum, dated September 5, 1972 and a credit advice dated September 5, 1972.

As Defendant's Exhibit No. 15, a credit advice, dated January 15, 1973, and a demand note, dated January 15, 1973.

As Defendant's Exhibit No. 16, a financial statement, dated February 27, 1973. That has already been submitted as Plaintiff's Exhibit No. 2.

As Defendant's Exhibit No. 17, a loan memorandum dated March 2, 1973, and a credit advice, dated March 2, 1973.

As Defendant's Exhibit No. 18, a promissory—discount note, dated June 1, 1973.

As Defendant's Exhibit No. 19, a promissory note dated November 1, 1973, which I believe is Plaintiff's Exhibit—

Mr. Webb: That is correct. Plaintiff's Exhibit No. 9.

The Court: Is that it, Mr. Crane?

Mr. Crane: I think I have a few more.

The Court: 20 is the next number.

Mr. Crane: 20 is a Group Exhibit consisting of a letter dated May 15, 1974, to the bankrupt from Carol King; a letter to Mr. Bishop of the Northern Trust, dated June 21, 1974, from James Carmel; and a memorandum or letter from the bankrupt, Ben F. Garman, to Northern Trust Company, dated January 15, 1975.

These are all from the loan file, and those are all of the documents.

The Court: As I understand, Mr. Webb, you stipulate as to the foundation for these documents? Admit and received in evidence, thank you.

Mr. Webb: Yes—no. We stipulate as to foundation.

Mr. Crane and I both agree that some documents we feel are not relevant.

The Court: Just the foundation.

Mr. Webb: Foundation, thank you, your Honor.

The Court: There may be objection as to relevance and that is reserved by both parties as to the other's documents.

Mr. Crane: Your Honor, I see that a young lady has entered. If that is plaintiff's second witness, I would

Mr. Crane: Yes, I do.

The Court: How long do you think your examination will last?

Mr. Crane: 45 minutes, I would guess.

The Court: All right. Then we will take a recess until 3:45.

(There was a short recess, after which the following further proceedings were had herein, to wit:)

The Court: We will continue with the complaint of Northern Trust Company vs. Ben F. Garman.

Are you ready to proceed, Mr. Crane?

Mr. Crane: Yes, your Honor.

Cross-Examination

By Mr. Crane:

Q. Mr. Bishop, you testified that on December 9, 1970, you were in charge of and made a loan to Ben F. Garman.

Do you recall to your own knowledge at that time how much Mr. Garman received in actual proceeds of that money?

A. No, sir.

Q. Do you know whether Mr. Garman received the full amount of that loan?

A. No, sir.

Q. If I were to say to you that a loan memorandum indicates that part of that loan paid off a prior account at Northern Trust, would that be correct?

A. I would have to look at the credit file to refresh my memory.

Q. Mr. Bishop, I shew you—would you mark this as—

The Court: You mark it, please.

It makes it go faster. In Federal Court, there is no magic to marking.

Mr. Crane: I think I have already indicated a date to this document as part of Defendant's Group Exhibit No. 11.

The Court: All right. You can make that "A", "B", "C", just tell me which one it is.

Mr. Crane: It is number A of Defendant's Group No. 11.

The Court: What document is it?

Mr. Crane: Purporting to be an interoffice memorandum dated December 9, 1970.

By Mr. Crane:

Q. Would you look at that document, Mr. Bishop, and tell me whether or not that bears your initials and your name on it?

A. Yes, sir, it does.

Q. Did you prepare that document?

A. Yes, sir.

Q. Would you read the portion of the document after the parties to whom it is addressed that says, "Re Ben F. Garman."

Would you read that for us?

A. Yes, sir. This is dated December 9, 1970.

(Reading:)

"I agreed to lend Mr. Garman $5,000 at 8 percent, repayable over a 14 month period.

"The purpose of the loan is to pay off his ACR line of approximately $3,000 and the remainder for personal expenses.

"Agreed upon repayment is as follows:

$1,000 within 183 days;

$1,500, 90 days beyond that point;

> $1,500 within 90 days of that date;
> and the remaining $1,000 90 days after that date."

Mr. Crane: That is sufficient.

The Witness: I have some other notes on there which change the repayment schedules somewhat.

By Mr. Crane:

Q. Would you please tell the Court what the ACR Account to be paid off is that you are referring to?

A. Those letters stand for "Automatic Cash Reserve" which is an overdraft facility on a checking account under which Mr. Garman owed the bank $3,000.

Q. When you made this memorandum of December 9, 1970, did you have the entire loan or credit file relating to Mr. Garman at Northern Trust Bank before you?

A. Yes, to the best of my knowledge.

Q. Did you have occasion to review that loan file?

A. Yes, sir.

Q. Do you know how many loans Mr. Garman had with the Northern Trust Company, how long it had a line of credit up to December 9, 1970?

A. Without checking the credit file, I don't know how long he had that ACR line.

Q. If I were to tell you that the credit file reflects an initial loan of January of 1972, would that appear to be correct?

A. No, sir.

The Court: Not '72.

Mr. Crane: '62, I'm sorry.

The Witness: '62? I said "No," in '72, because I had made loans prior to that.

I could verify that, I suppose, by looking through the credit file. It sounds reasonable that he could have borrowed back as early as '62.

By Mr. Crane:

Q. Were you aware of Mr. Garman's history or prior dealings with the Northern Trust on December 9, 1970?

A. Yes, I was aware of his relationship with us, the bank.

Q. Were you aware of the fact that Mr. Garman had approximately, at least two loans, for a period of 10 years or from January 1962, through December 9, 1970, two loans each year up to that time?

A. Am I aware of that today, or was I aware at the time?

Q. Are you aware of it now?

A. Not without rechecking the credit file.

Q. You did say that you were aware of his prior loans at the time that you made the loan in December, 1970?

A. I stated that I was aware of his relationship with the bank.

Q. On the bottom of that same form we have just looked at, the Defendant's Group Exhibit 11-A, there is a notation beginning 9/3/71.

Would you read that to the Court and explain what that meant?

A. This is in my handwriting. It is a note at the bottom of this typewritten memo that I read earlier. My handwritten note is dated 9/3/71 which says:

(Reading:)

"I agree to extend this loan for an additional 90 days—"

Then it has my initials, and below that I say:

"The balance as of 9/3/71 on the previously mentioned $5,000 loan is now $3,500...."

Below that I have noted:

"Renew on 9/10/71 for 90 days—"

Below that I have:

"Pay $1,500 on 12/10/71, and the balance of $2,000 on 3/10/72."

Q. Thank you.

Does that indicate or does that, to the best of your knowledge, mean that as of 9/3/71 that Mr. Garman's loan was extended for an additional 90 days?

A. Yes, sir.

Q. And does that mean that on December 10, 1971, Mr. Garman received an additional $1,500?

A. No, sir, that is a payment.

Q. Is that a payment?

A. Yes, sir.

Q. Did you receive any other documents from Mr. Garman on September 3, 1971, at the time of the extension of that loan?

A. Well.

Q. To your knowledge?

A. Not to my knowledge.

Q. Did you ask Mr. Garman for an additional personal financial statement form on September 3, 1971?

A. No, sir, not to my knowledge.

Q. Mr. Bishop, I now show you what is marked as Defendant's Exhibit No. 12, purporting to be a loan memorandum dated June 17, 1971, and ask you if that bears a facsimile of your signature and whether you prepared that memorandum?

A. Yes, sir. This is a copy of my signature; and the entire document, where it is handwritten, is my handwriting.

Q. And, would you tell the Court what loan that memorandum refers to?

Did that extend an original loan for another period of time?

A. Yes, sir. I have under purpose of loans, see loan memorandum dated 12/9/70 in the credit file.

Q. At that time, do you recall whether you took any additional documents or personal financial statements?

A. I recall that I did not since I had a 12th of December, '70 statement in my hands.

Mr. Crane: I ask that last portion of the answer be stricken, your Honor. That was not responsive to the question.

The Court: Yes?

Mr. Webb: Your Honor, maybe I misunderstood the question.

I thought it was completely responsive to the question.

The Court: So did I, Mr. Crane.

Therefore, your motion is denied.

Mr. Crane: Your Honor, I ask at this time that Defendant's Group Exhibit No. 11 and Defendant's Exhibit No. 12 be admitted into evidence.

The Court: Do you have any objection?

Mr. Webb: No, normally exhibits cannot be admitted on cross-examination.

The Court: That is correct.

Mr. Webb: I would state to the Court that simply means that Mr. Bishop would have to be called back again.

The Court: Not necessarily, if the proper foundation is made during the examination at the time, if it comes to pass, that the defendant goes ahead.

Then he could ask that they be admitted without Mr. Bishop being here.

Mr. Webb: I have allowed this witness to testify from the contents of these documents when they really aren't in evidence and I want to state for the record, I tend not to object so that it will make things speedier; I would ask the Court then to withhold ruling until Mr. Crane's chance to present his evidence when he can offer the exhibits and if they are relevant, it will not be necessary to call this witness back again.

The Court: All right.

So at this time, the Court will not rule on the admissibility of Defendant's Group Exhibit No. 11 or Defendant's Exhibit No. 12.

By Mr. Crane:

Q. Mr. Bishop, I call your attention to the loan made by Mr. Garman on December 21, 1971, about which you have testified.

Do you recall how much cash Mr. Garman was given at that time?

A. Would you repeat the date of that loan?

Q. December 21, 1971?

A. Well, there have been several notes here. I believe that was the one for $4,000 but I would like to take a look at the note to confirm that.

Mr. Crane: Your Honor, I have marked this document Defendant's Group Exhibit No. 13 and this is document A, a loan memorandum.

Mr. Bishop, I ask you if that loan memorandum was prepared by you and if that is in the same condition it was when you prepared it?

A. It appears to be other than the blue ballpoint notations at the bottom.

Q. That I have just written, Defendant's Group Exhibit?

A. Yes, sir.

Q. And, according to that memorandum, how much money did Mr. Garman receive on December 21, 1971?

A. You can't—

Q. Allow me to rephrase that, Mr. Bishop.

There is a section there that indicates $2,000 old loan, $4,000 new loan, would that be correct?

A. Yes, sir, but when you asked me how much he received, if it was a discounted note, he would get 3,900 and some odd dollars.

Q. So, the figures are approximate, is that correct?

A. Yes, sir.

Q. But, that indicates there was an existing balance at that time?

A. Yes, sir. Based on that, he received approximately a little under $4,000.

Q. And, the total amount of the note was how much, according to that document?

A. Well—

Q. What's the figure that you have written there?

A. $4,000.

Q. Do you have a total?

A. The total is 6. That would be the total of two notes, or it could be the total of just one note.

If we paid off the old $2,000 note, then I would like to check the file, but I would assume the new note is 6.

Since I just went over a $4,000 note, dated December 21, 1971, I conclude from that that there was an additional $2,000 note outstanding, the total indebtedness to the bank being $6,000.

Q. It could have been several notes?

A. I think there were two in this case.

Q. But the total indebtedness if I understand you was $6,000?

A. Yes, it was.

Q. And, at the time this $6,000 loan was made on December 21, 1971, and I show you Exhibit B of Defendant's Group Exhibit No. 13 For Identification purporting to be a credit advice, and ask you what that specific credit advice relates?

A. This relates that we credited what appears to be Mr. Garman's checking account 418137 at the Northern Trust Company.

Q. And, on what date was that account credited?

A. December 21, 1971.

Q. And, on December 21, 1971, did you take an additional personal financial statement from Mr. Garman during that date?

A. I requested an additional financial statement.

Q. Did you take one was the question that I asked you, on that date?

Did Mr. Garman present you on December 21, 1971, with an additional personal financial statement?

A. No, sir.

Q. Did he present you with an additional personal financial statement within the week prior to December 21, 1971?

A. No, sir.

Q. Now, I believe you testified, Mr. Bishop, that in January of 1973, Mr. Garman was given the proceeds of an additional loan for $15,000, is that correct?

A. Yes, sir.

Q. And, in January, 1973, were you the officer who approved that loan, if you recall?

A. Yes, I believe I was.

Q. And, in January 15, 1973, did you ask for or receive from Mr. Garman an additional personal financial statement?

A. I asked for an additional personal financial statement.

Q. Did you receive one at that time?

A. No, sir.

Q. Prior to this loan?

A. No, sir.

Q. And at the time the proceeds of the loan were credited to Mr. Garman's account, January 15, 1973, did you have an additional personal financial statement from Mr. Garman?

A. No, I had one dated December 22nd.

Q. No, I asked you if you had one dated that date?

A. Dated that date?

Q. Yes.

A. No, sir.

Q. Did you request one of Mr. Garman on that date?

A. Yes, sir.

Q. Did he give you one on that date?

A. No, sir.

Q. Did you proceed to transfer the money to his account on that date without the personal financial statement?

A. Based on his last financial statement that I did have.

Q. I am just asking you, did you credit him the $15,000?

A. Yes, sir.

Q. Calling your attention to March 2, 1973, I believe you testified that at that time you had been transferred, or were not in the bank, and that a Mr. Pero—

A. It's Perry R. Pero, P-E-R-O.

Q. Had authorized an additional loan to Mr. Garman, is that correct?

A. I testified that having looked at the note, it had his handwritten signature on it which indicates to me that he had approved it.

Q. Were you personally familiar with that loan on March 2, 1973?

A. No, I wasn't.

Q. Mr. Bishop, I show you a document marked Defendant's Group Exhibit 17 A, a loan memorandum dated March 2, 1973, and ask you based on this loan memorandum what was the amount of the loan made to Mr. Garman on March 2, 1973?

A. $5,000.

Q. And, what was the total amount of Mr. Garman's indebtedness to the bank on that date?

A. After that loan, $30,000.

Q. This is the loan that was made by Mr. Pero, is that correct?

A. Yes, sir.

Q. Now, would you please read for the Court, the comment written here as "Purpose of Loan"?

A. Yes, sir, it reads:

(Reading:)

"Cover miscellaneous expenses of moving into new home.

Mr. Bishop had agreed to make this loan prior to his transfer from the Eastern Division.

"If Mr. Garman has not sold his current home by June 1, 1973, I have agreed to renew the loan to 9/15/73."

Then, it just says "credit account, checking account."

Q. Do you recall that being your instructions?

A. No, sir.

Q. And, there was no additional personal financial statement requested or received of Mr. Garman on March 2, 1973, is that correct?

A. I have no idea.

Q. You have—there is none introduced by you, nor do we know. To your knowledge, do you know whether you asked him or he was asked about it?

A. I have no idea.

By The Court:

Q. Were you in charge of Mr. Garman's account on that date?

A. No, sir.

Q. When had you left?

A. Around January 12th, the 15th, about the middle of January.

Q. Of '73?

A. Yes, sir.

Q. Thank you.

By Mr. Crane:

Q. Mr. Bishop, did you ever take charge of Mr. Garman's account again after the date you just testified you left?

A. I would have to say that I believe there was a period of time following March, 1973, when Mr. Garman's loan

was administered by someone working for me in my new assignment.

In other words, this loan was moved from this Eastern Division referred to earlier to one of our Metropolitan lending divisions in which I was in charge.

By The Court:

Q. You had no personal knowledge of the loan administration during that period?

A. I think I would have, your Honor.

I may not have made the loans myself, but I would have been aware that he was borrowing from us.

By Mr. Crane:

Q. During the period of time of March, 1973, to the present time, did you ever personally consult with or talk to Mr. Garman relative to the account at the Northern Trust Company?

A. I think I probably did.

Q. Did you do that on the occasion where there was any loan made or additional monies requested?

A. No. It was an attempt to get some of it back.

Q. And, you contacted him, in other words, for collection purposes on old loans?

A. I don't remember the specific dates. I think I have had conversations with Mr. Garman subsequent to my direct lending to him with regard to outstanding loans.

Q. The additional loans that were made in March of '73, and the notes signed in June of '73, and November of '73, if I understand correctly, would have been either approved by some other officer or directly handled by someone else.

Somebody else would have been in contact with Mr. Garman?

A. That is correct.

Q. You weren't personally involved in the signing of the documents or a discussion of the extensions, or the renewal notes, with Mr. Garman?

A. Would you rephrase that question?

Q. Were you personally involved—were you present when Mr. Garman executed any of these notes?

A. Not to my knowledge, but I could have been.

I know Mr. Garman and if—

The Court: There is no question pending, sir.

By Mr. Crane:

Q. Mr. Bishop, I believe you testified that Mr. Garman did not list on his financial statements which you submitted as your exhibits the Exchange National Bank as a creditor, is that correct?

A. Yes, to the best of my knowledge.

Q. Do you know whether Mr. Garman had ever listed the Exchange National Bank on prior financial statements?

A. I do not know.

Q. Do you know whether the bank was aware of his relations with the Exchange National Bank prior to that time?

A. I was not when I was lending him money.

Q. If I were to tell you that the loan file contains memorandums referring to a loan at Exchange National Bank, would that be accurate.

You wouldn't know. I withdraw that question.

I show you a document labeled Defendant's Group Exhibit No. 1 A, dated January 12, 1962, which is part of the loan file, and ask you to read for the Court just that sentence right after "Re Ben Garman".

Mr. Webb: Your Honor, I am going to object on the grounds of relevancy.

The witness already testified he had no knowledge of the matters that took place in 1962.

First of all, it is clearly outside the scope of the direct, but more important than that, I would rather base it on the grounds of relevancy from the standpoint that it did

not have any relevancy to this witness' testimony as far as the events which he testified took place between the years 1970 and 1973.

He is now showing a document prepared by a third party which he did not prepare and asking questions about it.

The Court: As I understand it, Mr. Webb, this was part of the file.

I think the proper question to ask would be whether Mr. Bishop had knowledge of this particular document.

Mr. Crane: Well, your Honor, Mr. Bishop testified that he—

The Court: Well, you asked him to read from it. I think if you—

Mr. Crane: Mr. Bishop testified that he reviewed the loan file.

The Court: Surely, and you can ask him in his review whether he saw this document.

By The Witness:

A. No, sir, I don't recall it.

By Mr. Crane:

Q. Mr. Bishop, do you recall seeing a loan document dated November 27, 1963 interoffice memorandum when you reviewed the loan file?

The Court: While you are reading that, I should say that I am sustaining Mr. Webb's objection.

By The Witness:

A. I would have to answer by saying that here in 1977 I may have read this before.

I can't say specifically whether I have read this before or not. I may have but I don't remember. I didn't join the bank until 1966.

By Mr. Crane:

Q. You did review the loan file, is that correct?

A. Yes, I have reviewed the file.

That does not mean every single item in there. I was interested in the last couple of years when I was looking.

Q. Do you recall, Mr. Bishop, in your review of the file whether you came across or became familiar with a personal financial statement signed by Mr. Garman and dated October, 1964?

The Court: Have you given that an exhibit number, I don't recall?

Mr. Crane: No, I didn't.

By The Witness:

A. I do not recall whether I have seen that particular personal financial statement before or not.

Mr. Crane: That was Defendant's Exhibit No. 7, your Honor.

The Court: It has already been marked then.

By Mr. Crane:

Q. Mr. Bishop, you testified that when Mr. Garman made the loan of December 9, 1970, you reviewed his personal financial statement at that time?

A. Yes, sir.

Q. I believe you identified that personal financial statement as Plaintiff's Exhibit No. 2. Did you go over the items on this personal financial statement with Mr. Garman personally?

A. I don't think so.

Q. I show you what has been marked, this is a copy of a document marked Plaintiff's Exhibit No. 2, and ask you if you see under the section "Annual Income" "Other Income Counseling Fees?"

A. Yes, sir. I do.

Q. Did you ever ask Mr. Garman what that related to?

A. No, sir. I did not.

Q. Did you ever, at any time, instruct Mr. Garman in the filling out of this financial statement?

A. I don't believe so.

Q. Did you ever indicate to him what this financial statement was to be taken for?

A. I believe so.

Q. Did you ever tell him what his financial statement had to include or not include?

A. Oh, yes, sir.

Q. Do you know when you did that?

A. Specific date, no, sir, I don't.

Q. Mr. Bishop, is it accurate to say that in the course of Mr. Garman's dealing with the bank, from January of 1962, through November of 1973, you were personally involved with the making of the loan on December 19, 1970, and the loan January 15, 1973, and the extensions of loans in '71, is that correct?

Mr. Webb: Your Honor, I am going to object.

That question misstates the evidence as to what loans he was involved in.

Mr. Crane: It probably does.

The Court: I heard Mr. Crane say, "It probably does," therefore, the objection is sustained.

By Mr. Crane:

Q. Mr. Bishop, were you at the bank when Mr. Garman initially opened or had a loan with the Northern Trust Company?

A. I don't believe so.

Q. Are you at all personally familiar with any circumstances surrounding the opening of the loan at the Northern Trust Company?

A. I would say no.

Q. Are you familiar with any of the loans made by Mr. Garman or extensions thereof prior to December 9, 1970?

A. I would say probably so. Maybe some of the ones that may have been made in '66, '67, after I joined the bank because the loans were in the group that I happened to be a part of.

Q. Were you in charge of those loans at that time?

A. No, sir.

Q. Did you negotiate or were you personally involved in the making of those loans?

A. I think the first one I negotiated was the December 9, 1970, one.

Q. And did you familiarize yourself from the loan and credit file with all of the past loans and documents relating to his account?

A. No, sir. I would have only gone back a couple of years.

Q. Mr. Bishop, the only loan that you testified to in which a personal financial statement was taken contemporaneously with the loan was the one on December 9, 1970, is that right?

A. I think that's a fair statement.

Q. In making the loan to Mr. Garman on December 9, 1970, would you have reviewed this past loan record as a factor in making that loan?

A. At least the last few loans plus his most recent financial statement.

Mr. Crane: I have no further questions.

The Court: Do you have any further questions, Mr. Webb?

Mr. Webb: Just one or two, your Honor.

The Court: Surely.

By Mr. Webb:

Q. Mr. Bishop, I believe in response to one of Mr. Crane's questions, you stated that in December, 1970 you would not have reviewed the entire credit file but only the last couple of years as far as Mr. Garman's history with the bank is concerned, is that correct?

A. Yes, that's what I said.

Q. Would you tell the Court what the reason for that would be as to why you would only be interested in his most recent financial condition?

Mr. Crane: I object to that, your Honor.

He has already testified as to what he did at that time.

The Court: Well, we have to go into the state of mind of a person.

I think it is proper to have testimony as to the reasons that he would or would not do something at the time he was making his decision.

Therefore, the objection is overruled.

By The Witness:

A. I would only have gone back a couple of years as I stated principally because I was interested in what Mr. Garman owed the bank at the time I was considering the first loan I made on December 9th, what his current financial condition was not his financial condition several years ago, what his current income was as evidenced by the financial statement, so that I could judge as to his ability to repay the loan.

Other than for my information, general interest, there was no particular reason to examine the file in detail more than the last couple of years.

By Mr. Webb:

Q. Thank you, Mr. Bishop. Now, one other question.

Mr. Crane in his questioning asked you if in fact that December 9, 1970, loan was the only loan where you had contemporaneously had a financial statement, I believe it was dated one day before that on December 8th.

Mr. Crane asked you a series of questions about the dates on these financial statements. I am going to ask you based on your experience as an officer of the Northern Trust Company, would you tell the Court what in your judgment would be considered for the purposes of making a loan or additional loan to a customer, a current financial statement on which you could rely?

Mr. Crane: I will object to that as to what the practice or his normal—

Mr. Webb: I think he opened this up with his questions as to whether it was reasonable for him to rely upon certain statements that were in the bank's files at the time that he made certain loans after December, 1970.

So, I think that his judgment and reasonableness as far as his reliance is concerned has been presented to the Court.

Mr. Crane: I never asked if it was reasonable. I asked if he reviewed the files.

The Court: That's right. There has been no issue as to reasonableness.

I think that is ultimately an issue that will be decided by the Court, but the form of the question is objectionable and the objection is sustained.

Mr. Webb: To that line of inquiry?

The Court: Not to that, never to a line of inquiry. You may always go ahead until such time as someone says, "All right, you have asked that before, Mr. Webb."

By Mr. Webb:

Q. Well, let me ask you this: Did you consider the financial statements that you relied upon for the years 1970, 1971, 1972, and 1973 to be current for your specific purpose in loaning money to Mr. Garman?

Mr. Crane: I will object to that, your Honor, categorizing statements he relied on.

The Court: I think that is argumentative. That is a fact that must be determined by the Court regardless of whether this officer may feel it is current.

Mr. Webb: I have no further questions, your Honor.

By The Court:

Q. As to this statement that was made on December 8, 1970, you said you looked back to the file for a couple of years, did you verify Mr. Garman's employment at that time?

A. No, sir, because I was familiar with the company and his superior in Chicago. I knew he was employed by that firm so I did not have to verify it.

Q. Did you verify how many dependents Mr. Garman had at that time?

A. No, sir. That was essentially irrelevant based on his income level and financial condition in terms of our loan.

Q. His net worth is the basis on which you make all of these decisions?

A. That coupled with the income, current indebtedness, in other words, his cash flow, his ability to repay the loan.

Q. All right. I am interested, and you will have to bear with me while I formulate some of these.

The cash flow shows $37,000. Is that gross income or net income?

A. That was the gross, I believe, yes, sir.

Q. You have to take out taxes from that?

A. Yes, living expenses and mortgage and so forth.

Q. Don't you come to some judgment, or some figure that you look to as to the monies that are available to repay any indebtedness?

A. Yes, sir.

Q. Did you, as to the December 8, 1970, statement?

A. Yes, sir.

Q. What was that figures?

I have a copy of here, that has been identified as Exhibit No. 2, you have $37,000 as total income?

A. Yes, sir.

Q. His net worth—I suppose what I am getting into, Mr. Bishop, the net worth here all seems to be tied up in a particular house?

A. Yes, sir, 39 from 75, the bulk of it.

Q. That is not very liquid?

A. No, sir, but with a $37,000 income, there should be sufficient monies to repay the loans.

Q. How much money do you think from that he had to repay the loans in 1970?

Why didn't you get a statement as to his monthly mortgage payment. It is not there, is it?

A. No, sir.

Q. What the school costs; do his children have school expenses?

A. That is an excellent idea.

Q. This is what I look to. I don't consider that necessarily a financial statement because it doesn't show the monthly income and expenses.

It may be a financial statement in the sense that it may be assets and liabilities, but somehow these are misleading, even if we assume that they were stated accurately as to what a cash position of a person is and what types of loans he can handle.

A. Of course, when we talk with a borrower, we set up a repayment schedule that meets his abilities that indicates quite a bit in terms of funds—

Q. These weren't monthly payments?

A. No, sir.

Q. It doesn't show that he has any cash on hand. He had an overdrawn checking account. So, where do you think the cash is going to come from to pay these loans?

A. His monthly or bimonthly payments from the company he work for.

Q. How do you know for any monthly or bimonthly payment that there would be funds available to pay the loan?

A. From the statement?

Q. Yes.

A. You can't tell from the statement.

Q. That's right.

The Court: Did you wish to ask Mr. Bishop any questions?

This bothers me on these types of statements.

Mr. Crane: Your Honor, may I recall Mr. Bishop later and ask just a few more questions?

You have asked him about the company that Mr. Garman is employed by which I think requires, for the benefit of the Court, an explanation from Mr. Bishop.

The Court: Why? I was just wondering if he verified this from the file or some other place, that is all.

It does bother me, Mr. Webb, and— Do we have any more quetsions of Mr. Bishop?

Mr. Crane: I do.

The Court: Of what basis?

Mr. Crane: I would like Mr. Bishop to tell the Court what company Mr. Garman does work for.

The Court: New York Life. It says on the financial statement.

Mr. Crane: And whether New York Life is a major depositor in an account with the Northern Trust Company?

The Court: It may very well be.

Mr. Crane: And whether Mr. Garman was given a loan at the request of the New York Life Insurance Company?

By The Witness:

A. Not by me.

The Court: There is an answer.

By The Witness:

A. In other words, any loans I made were not requested by New York Life. They were requested by Mr. Garman.

The Court: Do you have any more questions of Mr. Bishop?

Mr. Webb: I have no further questions, your Honor.

The Court: Do you have any other questions?

Mr. Crane: I have no questions.

The Court: All right, thank you, Mr. Bishop.

You may talk to Mr. Bishop afterwards, after my comments but this bothers me that you expect a person to be able to save $5,000 in a period of time or make payments of $1,000 in a particular time.

There is no way to analyze his income to determine whether he will have the cash on hand.

By The Witness:

A. Since your Honor is interested in that particular point, and I think it is a good one, I would tell you that on normally installment loans that information is available and—

The Court: Yes, I know it is.

By The Witness:

A. On the larger loans where the borrowers of more substantial means is indicated by his financial statement, I think that perhaps we have been somewhat remiss in not taking those things, specific expense numbers, down.

The Court: It seems to me that whether there is an installment loan or a loan like this, there has to be some way to judge that.

Mr. Webb and I will work that out later on.

Thank you, Mr. Bishop.

(Witness excused.)

The Court: Do you wish to call Ms. King?

Mr. Webb: I spoke to her and told her that she might have to come back tomorrow because of the timing and she said that was fine.

The Court: How much time will it take?

Mr. Webb: Well, my direct is not very lengthy. I don't know how long cross is.

The Court: Call her in.

Mr. Crane: I couldn't be very long.

The Court: Why don't we try to get this part of the

No. 80-442

NOV 2

In the Supreme Court of the United States

OCTOBER TERM, 1980

BEN F. GARMAN,

Petitioner,

vs.

THE NORTHERN TRUST COMPANY,

Respondent.

REPLY MEMORANDUM

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TABLE OF CONTENTS

	PAGE
Preface	1
Reply	2-8
Conclusion	9
Appendix	
Judge James' minute order	App. 1
Portion of Transcript of Proceedings in Bankruptcy Court on March 29, 1977	App. 2
Portion of Transcript of Proceedings in Bankruptcy Court on March 28, 1977	App. 3

TABLE OF AUTHORITIES

Cases

PAGE

Engstrom v. Wiley, 191 F.2d 684 (9th Cir. 1951) 6

Haynes v. United States, 390 U.S. 85 (1968) 8

Kostelac v. United States, 247 F.2d 723 (9th Cir. 1957) 5

Kosty v. Lewis, 319 F.2d 744 (D.C. Cir. 1963) 8

Magna Sales Co. v. Magna Alloys Research Pty., 545 F.2d 668 (9th Cir. 1977) 5

Mayor of Philadelphia v. Educational Equality League, 415 U.S. 605 (1974) 6

In re Rockford Baseball Club, 201 F.2d 685 (7th Cir. 1953) 7

Singleton v. Wulff, 428 U.S. 121 (1976) 7

Smith v. Dravo Corp., 208 F.2d 388 (7th Cir. 1953) 5

Yunker v. CIR, 256 F.2d 130 (6th Cir. 1958) 5

Constitution, Statutes and Rules

Bankruptcy Act, 11 U.S.C. §35 U.S.C. §35(a)(2) 3, 4

28 U.S.C §2106 4

Rule 41(b), Federal Rules of Civil Procedure 1, 2, 3, 4, 8

Rule 52(a), Federal Rules of Civil Procedure 4, 7

Other Authorities

5 J. Moore, Federal Practice §41.13[2] at 41-185 (2d ed. 1980) 4

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REPLY MEMORANDUM

Preface

The response to the Petition for a Writ of Certiorari was astutely drafted using a devious design of distraction from the real issues and derangement of the facts in the hope of so muddling this appeal as to create some grand delusion. While speaking out against "jaundiced partnership," the respondent seeks to influence this Court with its diatribe of remarks of "criminality," "student of semantics," and other unfounded innuendoes about the petitioner.

Rather than addressing itself to Rule 41(b) of the Federal Rules of Civil Procedure, and the due process issues, the respondent merely glosses over these matters, relegating its response to petitioner's cases to footnotes, and

spends the majority of its brief with its own biased version of the facts.

At no place in its brief does the respondent support its underlying premise with case law or otherwise, that the limited testimony of a defendant as an adverse witness somehow satisfies the requirements of Rule 41(b) of the Federal Rules of Civil Procedure. While desiring to avoid the pitfalls of the expertly laid snare of diversion, the petitioner must respond to the respondent's brief.

A.

The respondent, Northern Trust Company, in its response to the Petition for Writ of Certiorari, has continued in its practice of engaging in the most virulent obfuscation of the factual situation in making allegations as if true, while the record bears clear and cogent evidence of denial of due process. They do not address themselves to petitioner's cases or argument.

Respondent's allegation in its brief that a "plenary trial" on the issue of dischargeability was held insinuates that a *full* trial was held. The statement ignores the facts that only the plaintiff proceeded and that the defendant moved for a dismissal at the close of plaintiff's case. The record shows that defendant had over 20 group exhibits (the foundation for which was stipulated)[1] which he intended to introduce and which would have established the true relationship between Northern Trust Company and Ben Garman. Had his motion been denied, the defendant would have also had the opportunity to call as witnesses the "claimants" listed in his bankruptcy schedules to corroborate his testimony.[2]

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[1] App. Trans. pages 1 through 5.

[2] Garman testified that these claims were only listed at the insistence of his attorneys and did not represent any indebtedness. (See Appendix).

Respondent ignores the finding of the bankruptcy judge,[3] and avoids the finding of the district court judge affirming the bankruptcy judge's decision, (Appendix, page 11) wherein the district court judge correctly noted that the bankruptcy judge did not rule on the issue of whether a prima facie case had been made or whether Garman had the requisite "intent to deceive." Judge James' decision was made solely on the one element of whether reasonableness of reliance existed. There was no ruling upon the other elements of fraud necessary to bar the dischargeability of Ben Garman as required by 17(a)(2) of the Bankruptcy Act, (11 U.S.C. 35a(2)). Ben Garman, petitioner herein, did not have a chance to offer evidence in his own behalf. The "direct" examination referred to was as an adverse witness and limited solely to the questions raised by plaintiff's attorney. The 20 group exhibits referred to in Appendix 1 through 5 were never admitted into evidence. The witnesses to substantiate these documents and the general nature of the transactions were never allowed to testify because petitioner relied on Rule 41(b) in his right to put in a full and complete defense with all of his testimony and exhibits, had his motion been denied. The fact that his motion was successful should not bar him from so defending, if indeed the burden had shifted his case.

The "inherent incredibility," if any, is the testimony of Mr. Bishop, witness for the Northern Trust, and its other witness in over 12 years of lending and making loans to Ben Garman, the petitioner. Its primary reliance in making the last loan in November of 1973 was a written statement demanded 5 months *after* the loan was actually made, and only for the bank's benefit, at the bank's request, be-

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[3] App. pp. 9 and 10.

cause they were required to keep loans that were six months past maturity up to date or renewed.[4]

The testimony of Northern Trust's officers was that no financial statement (except one in 1970) was ever demanded or taken prior to or contemporaneaus with any loan. An alleged oral statement was made that Garman's financial condition was materially unchanged, but no reference *ever* was made regarding prior written statements. Section 17(a)(2), *11 U.S.C. 35(a)(2)*, demands that a false financial statement be in writing and any republication thereof be in writing, and that they must be made at the inception of the loan.[5]

B.

The respondent supplements its version of the facts with rhetoric about how Rule 52(a) of the Federal Rules of Civil Procedure and 28 U.S.C. §2106 justifies the decision of the court of appeals. However, crucial to the interpretation of these sections and disregarded by the respondent in its very own quotation (5 J. Moore, Federal Practice §41.13(2) at 41-185 (2nd Ed. 1980), respondent's brief, p. 14) is the requirement of the existence of undisputed facts or the presentation of *all* of defendant's evidence at trial prior to a proper appellate court reversal without remand. The paper shield respondent hides behind is insufficient to stymie petitioner's due process arguments and Rule 41(b) violations present in this cause. Respondent's own cited cases do not support its premise that an appellate court can become the fact-finder where disputed facts exist, and where the defendant has not had the opportunity to present his case in chief.

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[4] App. Trans. 88, 89, 90.

[5] 1A Collier on Bankruptcy, Sec. 17.16, pp. 1638.

Smith v. *Dravo Corp.*, 208 F.2d 388 (7th Cir. 1953, cited by the respondent, states that where the record is complete or the evidence uncontradicted or entirely documentary, the Appellate Court may decide the case. The court specifically restricted the use of its role as a fact finder in cases which did not involve witnesses' credibility, (at 392):

> "In McComb v. Utica Knitting Co., 2 Cir. 164 F.2d 670, at page 674, the court, after observing that the trial judge did not discuss a certain question or make any findings on it, citing a number of cases, said: 'As that evidence is entirely documentary, *no issue of witness' credibility arises;* therefore, we can pass on the facts as well as could the trial judge, and need not remand for a finding by him.' (emphasis added.)
>
> "In view of these authorities *and of the nature of the proof and its complete character,* we have entered our conclusions as to plaintiffs devices ABCD,E and F-G, as to the capital loss investment and as to interest, thus eliminating the necessity of any further hearing as to them." (emphasis added.)

In *Magna Sales Co.* v. *Magna Alloys Research Pty,* 545 F.2d 668 (9th Cir. 1977), cited by the respondent, the Court of Appeals cautioned against an appellate court making its own findings and stated the proposition that the failure of a trial court to issue separate findings "does not demand reversal" (at 671).

Yunker v. *CIR,* 256 F.2d 130 (6th Cir. 1958) and *Kostelac* v. *United States,* 247 F.2d 723 (9th Cir. 1957) also cited by respondent, were both cases in which there were undisputed facts consisting of documentary evidence. In the latter cause the appellate court made this perfectly clear:

> "Since the court has made no findings and since the evidence on this question is written, as it was before the trial court, it is proper for this court from such undisputed written evidence to decide whether Kostelac was entitled to rescind the contract . . . ." (at 726).

Another equally interesting Ninth Circuit case which the respondent failed to cite is *Engstrom* v. *Wiley,* 191 F.2d 684 (9th Cir. 1951). There the appellate court hesitated to determine its own findings of fact even where the facts were stipulated (at 686):

> "At the outset, it is urged that, since the facts are stipulated, this court must necessarily arrive at a result by consideration of the facts de novo. No such authority is vested in this court. The trial judge has found the facts. The function of this court is to determine whether his findings are unsupported by substantial evidence and therefore clearly erroneous."

Are we faced with a situation falling within the guidelines of the quotation of the respondent? (Respondent's brief, p. 14). The evidence is certainly not entirely documentary when the question of intent to deceive and fraud is involved. All of the evidence in the record is certainly not complete when neither the defendant's exhibits have been introduced nor has he had an opportunity to present them in his defense. The evidence is certainly not uncontradicted, entirely documentary, or complete, when the defendant has been unable to introduce witnesses relating to the particular debts alleged. Furthermore, the credibility of a witness is directly at issue.

As this court expressed in *Mayor of the City of Philadelphia* v. *Educational Equality League,* 415 U.S. 605 (1974), credibility of witnesses is difficult to determine from a transcript and better reserved with the trial judge (at 622):

> "We share the view expressed in the dissent [415 US at 645] that facts in a case like the instant one, 'when seen through the eyes of judges familiar with the context in which they occurred, may have special significance that is lost on those with only the printed page before them' . . . ."

In *In re Rockford Baseball Club,* 201 F.2d 685 (7th Cir. 1953), the appellate court recognized the import of refraining from judging the credibility of witnesses where the trial judge made no specific findings pursuant to Rule 52(a) (at 687):

> "The record, therefore, reveals a situation aptly suited to the referee's function, that is, of passing on the credibility of witnesses and the reliability of their testimony, and of then selecting that evidence which to him seemed most reliable as a basis for findings of fact. Since we are not apprised of his subsidiary findings, 'we are far asea as to the exact factual basis upon which the judgment was founded.' Maher v. Hendrickson, 7 Cir., 188 F.2d 700, 702.
>
> "As the Supreme Court stated in Kelly v. Everglades Drainage District, 319 U.S. 415, at pages 421-422, 63 S.Ct. 1141, at pages 1145, 87 L.Ed. 1485:
>
> > It may be that adequate evidence * * * is in the present record. On that we do not pass, for it is not the function of this court to search the record and analyze the evidence in order to supply findings which the trial court failed to make. * * * the nature of the evidentiary findings sufficient and appropriate to support the court's decision * * * is for the trial court to determine in the first instance in the light of the circumstances of the particular case. We hold only that there must be findings * * * which are sufficient to indicate the factual basis for the ultimate conclusion.' "

Nor has respondent demonstrated that this is one of those cases where its resolution is beyond any doubt or where "injustice might otherwise result." In the very case cited by respondent in this regard, *Singleton* v. *Wulff,* 428 US 106 (1976), this Court found those requisites absent and reversed the action of the court of appeals with language quite relevant to the instant cause (at 120):

> "It is the general rule, of course, that a federal appellate court does not consider an issue not passed

> upon below. In *Hormel* v. *Helvering,* 312 U.S. 552, 556 (1941), the court explained that this is 'essential in order that parties may have the opportunity to offer all the evidence they believe relevant to the issues . . . [and] in order that litigants may not be surprised on appeal by final decision there of issues upon which they have had no opportunity to introduce evidence.' We have no idea what evidence, if any, petitioner would, or could, offer in defense of this statute, but this is only because petitioner has had no opportunity to proffer such evidence."

The other two cases cited by respondent in support of its contention that this cause should not be remanded, *Haynes* v. *United States,* 390 U.S. 85 (1968), and *Kosty* v. *Lewis,* 319 F.2d 744 (D.C. Cir. 1963) are clearly distinguishable from the instant matter. The former case involved a claim of privilege against self-incrimination which was held to be a complete defense to the charges against the defendant resulting in an "inevitable" reversal of his conviction. In the latter case the defendant "expressly admitted" that it had no evidence to rebut the plaintiff's claims. Contrarily, in the instant matter, the petitioner contends it has proof to offer in his defense and the result is by no means "inevitable."

CONCLUSION

The cases cited in the various briefs clearly indicate that Ben Garman, the petitioner herein, has been denied an opportunity to present his defense. He has not been allowed to introduce documentary evidence, testify on his own behalf, or call witnesses to rebut an allegation of fraud which had not been proved in all of its elements. The record, replete with conflicting testimony, can only be balanced by an opportunity to allow a proper defense. Reliance on Rule 41(b) of the Rules of Federal Procedure cannot be cast aside simply for the sake of expediency coupled with

innuendoes of guilt; this is precisely what our rights of due process insure against.

For the foregoing reasons, Ben Garman, the petitioner herein, respectfully requests that the Petition for Certiorari be granted.

DANNEN, CRANE, HEYMAN & HAAS
By: Eugene Crane
Mitchell A. Cohen
Attorneys for Petitioner

APPENDIX

APPENDIX

Judge James' minute order

UNITED STATES DISTRICT COURT,
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

Name of Presiding Judge, Honorable Thomas James

Cause No. 75 B 1111 Date March 29, 1977
Title of Cause Ben F. Garman

Northern Trust Company, plaintiff

vs.

Ben F. Garman, defendant

This case come on for trial on the complaint of the Northern Trust Company, plaintiff, to determine the dischargeability of an alleged debt owed it by Ben F. Garman, defendant. After the plaintiff had completed the presentation of its evidence, the defendant moved for dismissal of the complaint on the ground that upon the facts and the law the plaintiff had shown no right to relief (Bankruptcy Rule 741). For the reasons stated in open court on March 29, 1977, this court granted defendant's motion to dismiss. Judgment is therefore entered in favor of Ben F. Garman, defendant-bankrupt, and against Northern Trust Company, plaintiff, and the complaint and cause of action stated in it are dismissed.

cc Mr. Eugene Crane
Mr. Daniel Webb

Portion of Transcript of Proceedings in Bankruptcy Court on March 29, 1977

reliance on a particular document where nothing else can be seen from the fact that a balance existed, that there was a course of conduct. There had to be. The balance was from some loan, prior loan, that had been made for whatever reason it had been made and credit had been granted at that time.

So, the reliance is not on that one statement or a supposed republication in the statement because of the wording that said something to the effect that anybody signing that statement would advise the bank if a condition changes which I consider as a practical matter to be almost ludicrous, and in subsequently making loans and taking additional statements after the loan, in choosing the one on which to rely because it is contemporaneous as the only contemporaneous statement indicates that there cannot have been any reliance on these statements at all.

I submit that the elements of moral turpitude and fraud in the denial of a discharge have not been met.

The Court: Thank you.

In all of these cases under Section 17(a) the Court requires clear and convincing evidence at some point. I do not think at this point when the motion is made that the Court should go ahead with a trial if it believes that the evidence is not clear and convincing so at the end of the defendant's case it could render a judgment in favor of the plaintiff.

Therefore, I shall grant the motion to dismiss at this time.

The plaintiff has not proven by clear and convincing evidence that it would be entitled on the facts and the law to a judgment in its favor.

I note that Section 17(a) provides in pertinent part, that is sub-section two, a discharge in bankruptcy shall release a bankrupt from all of his proven debt except such as are for obtaining money or property on credit, or obtaining an extension or renewal of credit in reliance on a materially false statement in writing respecting his financial condition, made or published, or caused to be made or published in any matter whatsoever with intent to deceive.

I appreciate Mr. Webb's comments about Mr. Garman's testimony though I think that your comments, Mr. Webb, do not necessarily state that or show that Mr. Garman did have the intent. However, I do not make my judgment on whether there was intent to deceive in this case. I looked more to the conduct of

Portion of Transcript of Proceedings in Bankruptcy Court on March 28, 1977

relied upon in making certain loans of money to Mr. Garman.

The loans totaled $30,000 during the years 1970, 1971, 1972, and 1973. As of November 1, 1973, the loans totaled $30,000. At that time Mr. Garman signed a renewal note for the $30,000.

The bank relied upon the most recent financial statement on file with it at that time. In January, 1975, the defendant Ben F. Garman, filed a petition in bankruptcy with this Court, and in that petition listed on Schedule A-3 marked "unsecured debts", listed approximately $50,000 in debts which he stated on the bankruptcy petition had been in existence at the time he filed the written financial statements with the bank, but which debts were not included upon the written financial statements filed with the bank during the years '70 through '73.

I anticipate in proving that the bank had in its possession these false financial statements, relied upon them to their detriment, loaned the $30,000 to Mr. Garman, and now Mr. Garman has filed the petition in bankruptcy to have this debt discharged.

It is the plaintiff's contention that under the appropriate statute referred to in our complaint that because this debt was based upon a false written

As its Group Exhibit No. 1, all of these documents are copies of documents in the bank's loan or credit file which I got from the plaintiff pursuant to motion to produce, the Defendant's Group Exhibit No. 1 which consists of an interoffice memorandum dated January 12, 1962; a loan memorandum dated January 12, 1962; a letter from the Northern Trust, dated January 15, 1962, to Mr. Hugh Fanning; and an undated memo signed GSS which Mr. Webb would agree appears to be part of that same dated transaction.

Mr. Webb: That is correct.

Mr. Crane: As Defendant's Exhibit No. 2, an interoffice memorandum from the Northern Trust, dated November 27, 1963.

As Defendant's Exhibit No. 3, an interoffice memorandum dated January 21, 1964.

As Defendant's Exhibit No. 4, consisting of two documents, I'm sorry, one document with two notations, a note from Ben Garman, the bankrupt, dated 7/3/64; and a hand-written response, dated 7/8/63, I think there is an error in the date, to that by the bank.

Is that correct, Mr. Webb?

Mr. Webb: Yes, that is correct.

Mr. Crane: As Defendant's Exhibit No. 5, an interoffice memorandum, dated June 15, 1967, and a loan memorandum dated, June 14, 1967.

As Defendant's Exhibit No. 6, a personal financial statement, dated January 5, 1962.

The Court: These all go in chronological order?

Mr. Crane: No, I'm sorry, your Honor, they go back at the moment.

The Court: Is that January 5, 1962?

Mr. Crane: Yes, sir.

As No. 7, a financial statement, dated October 22, 1964.

As No. 8, a financial statement, dated May 18, 1966.

No. 9, a financial statement, dated June 22, 1967.

No. 10, a financial statement, dated December 9, 1968.

Defendant's Group Exhibit No. 11, which consists of 5 documents, an interoffice memorandum, dated December 9, 1970, which bears on it a notation on it dated, September 3, 1971, it is apparently two documents in one; a loan memorandum, dated December 9, 1970; a personal financial statement, dated December 8, 1970; and a credit advice, dated December 9, 1970.

As Defendant's Exhibit No. 12, a loan memorandum dated June 17, 1971.

Defendant's Exhibit No. 13, consisting of 3 documents, a loan memorandum, dated December 21, 1971; a credit advice, dated December 21, 1971; and a personal financial statement, dated December 22, 1971.

Defendant's Exhibit No. 14, a loan memorandum, dated September 5, 1972 and a credit advice dated September 5, 1972.

As Defendant's Exhibit No. 15, a credit advice, dated January 15, 1973, and a demand note, dated January 15, 1973.

As Defendant's Exhibit No. 16, a financial statement, dated February 27, 1973. That has already been submitted as Plaintiff's Exhibit No. 2.

As Defendant's Exhibit No. 17, a loan memorandum dated March 2, 1973, and a credit advice, dated March 2, 1973.

As Defendant's Exhibit No. 18, a promissory—discount note, dated June 1, 1973.

As Defendant's Exhibit No. 19, a promissory note dated November 1, 1973, which I believe is Plaintiff's Exhibit—

Mr. Webb: That is correct. Plaintiff's Exhibit No. 9.

The Court: Is that it, Mr. Crane?

Mr. Crane: I think I have a few more.

The Court: 20 is the next number.

Mr. Crane: 20 is a Group Exhibit consisting of a letter dated May 15, 1974, to the bankrupt from Carol King; a letter to Mr. Bishop of the Northern Trust, dated June 21, 1974, from James Carmel; and a memorandum or letter from the bankrupt, Ben F. Garman, to Northern Trust Company, dated January 15, 1975.

These are all from the loan file, and those are all of the documents.

The Court: As I understand, Mr. Webb, you stipulate as to the foundation for these documents? Admit and received in evidence, thank you.

Mr. Webb: Yes—no. We stipulate as to foundation.

Mr. Crane and I both agree that some documents we feel are not relevant.

The Court: Just the foundation.

Mr. Webb: Foundation, thank you, your Honor.

The Court: There may be objection as to relevance and that is reserved by both parties as to the other's documents.

Mr. Crane: Your Honor, I see that a young lady has entered. If that is plaintiff's second witness, I would • • •

Q. It wouldn't be after?

A. No, sir.

Q. What I am getting to is did you have the personal financial statement dated December 22, 1971 at the time you made the loan to Mr. Garman?

A. No, your Honor.

Q. Thank you.

By Mr. Webb:

Q. Now, directing your attention to—

The Court: I think I interrupted his answer.

By Mr. Webb:

Q. Were you in the middle of explaining what you did in this particular case as to that particular $4,000 loan?

A. Yes, I was.

Q. Would you please continue.

A. I left off at the point of indicating that I had examined the December 8, 1970 statement previously presented to me and that I had asked Mr. Garman if there had been any material change in his financial condition since that date.

I would have asked this question on or a few days prior to December 21, 1971. I approved this loan based on the 12/8/1970 financial statement, and Mr. Garman's * * * loan that is reflected on the exhibit marked Plaintiff's Exhibit No. 5?

Mr. Crane: Your Honor, I will object to that.

That calls for a conclusion of the witness as to what he did with the documents 2, 4, and 7. Maybe he did nothing with them.

The Court: That's right, and he can so state.

That is a proper question and the objection is overruled.

By The Witness:

A. In connection with the loan that I made to Mr. Garman in the amount of $10,000 on September 5, 1972, I examined the most recent financial statement which I had in my possession which was dated December 22, 1971.

Based upon this financial statement, together with Mr. Garman's statement, oral statement to me, that there had been no change in his financial condition at the time of this loan, September 5, 1972 back to December 22, '71, I granted this additional loan.

By Mr. Webb:

Q. Now, directing your attention to the exhibit marked as Plaintiff's Exhibit No. 6 which was previously identified as a note for $15,000, dated January 15, 1973, do you have that in your hand and are you looking at that at this time, Mr. Bishop?

A. Yes, I am.

Q. I want you to examine Plaintiff's Exhibit Nos. 2, 4, and 7, the financial statements and tell the Court what if anything you did with those statements in connection with the loan evidenced by Plaintiff's Exhibit No. 6?

A. In the case of the $15,000 loan, dated January 15, 1973, to Mr. Garman, I referred to the December 22, 1971 financial condition; re-examined it; asked Mr. Garman again if there had been any material change in his financial condition since December 22, 1971, and the time I made this loan on January 15, 1973.

He indicated there had not been any material change. Upon—I made my loan decision based on that and asked him to resubmit a more current personal financial statement which he subsequently did about a month later, dated February 27, 1973. That's the financial statement.

Q. Now, Mr. Bishop, you might lay those exhibits aside, but would you please keep the financial statements in your hand.

Prior to testifying here today, have you seen the bankruptcy petition filed in this case designated * * *

Q. Is that a payment?

A. Yes, sir.

Q. Did you receive any other documents from Mr. Garman on September 3, 1971, at the time of the extension of that loan?

A. Well.

Q. To your knowledge?

A. Not to my knowledge.

Q. Did you ask Mr. Garman for an additional personal financial statement form on September 3, 1971?

A. No, sir, not to my knowledge.

Q. Mr. Bishop, I now show you what is marked as Defendant's Exhibit No. 12, purporting to be a loan memorandum dated June 17, 1971, and ask you if that bears a facsimile of your signature and whether you prepared that memorandum?

A. Yes, sir. This is a copy of my signature; and the entire document, where it is handwritten, is my handwriting.

Q. And, would you tell the Court what loan that memorandum refers to?

Did that extend an original loan for another period of time?

A. Yes, sir. I have under purpose of loans, see * * *

Q. But the total indebtedness if I understand you was $6,000?

A. Yes, it was.

Q. And, at the time this $6,000 loan was made on December 21, 1971, and I show you Exhibit B of Defendant's Group Exhibit No. 13 For Identification purporting to be a credit advice, and ask you what that specific credit advice relates?

A. This relates that we credited what appears to be Mr. Garman's checking account 418137 at the Northern Trust Company.

Q. And, on what date was that account credited?

A. December 21, 1971.

Q. And, on December 21, 1971, did you take an additional personal financial statement from Mr. Garman during that date?

A. I requested an additional financial statement.

Q. Did you take one was the question that I asked you, on that date?

Did Mr. Garman present you on December 21, 1971, with an additional personal financial statement?

A. No, sir.

Q. Did he present you with an additional personal financial statement within the week prior to * * *

The Court: Have you given that an exhibit number, I don't recall?

Mr. Crane: No, I didn't.

By The Witness:

A. I do not recall whether I have seen that particular personal financial statement before or not.

Mr. Crane: That was Defendant's Exhibit No. 7, your Honor.

The Court: It has already been marked then.

By Mr. Crane:

Q. Mr. Bishop, you testified that when Mr. Garman made the loan of December 9, 1970, you reviewed his personal financial statement at that time?

A. Yes, sir.

Q. I believe you identified that personal financial statement as Plaintiff's Exhibit No. 2. Did you go over the items on this personal financial statement with Mr. Garman personally?

A. I don't think so.

Q. I show you what has been marked, this is a copy of a document marked Plaintiff's Exhibit No. 2, and ask you if you see under the section "Annual Income" "Other Income Counseling Fees?"

A. Yes, sir. I do.

By Mr. Crane:

Q. Mr. Bishop, I believe you testified that Mr. Garman did not list on his financial statements which you submitted as your exhibits the Exchange National Bank as a creditor, is that correct?

A. Yes, to the best of my knowledge.

Q. Do you know whether Mr. Garman had ever listed the Exchange National Bank on prior financial statements?

A. I do not know.

Q. Do you know whether the bank was aware of his relations with the Exchange National Bank prior to that time?

A. I was not when I was lending him money.

Q. If I were to tell you that the loan file contains memorandums referring to a loan at Exchange National Bank, would that be accurate.

You wouldn't know. I withdraw that question.

I show you a document labeled Defendant's Group Exhibit No. 1 A, dated January 12, 1962, which is part of the loan file, and ask you to read for the Court just that sentence right after "Re Ben Garman".

Mr. Webb: Your Honor, I am going to object on the grounds of relevancy.

any loan made or additional monies requested?

A. No. It was an attempt to get some of it back.

Q. And, you contacted him, in other words, for collection purposes on old loans?

A. I don't remember the specific dates. I think I have had conversations with Mr. Garman subsequent to my direct lending to him with regard to outstanding loans.

Q. The additional loans that were made in March of '73, and the notes signed in June of '73, and November of '73, if I understand correctly, would have been either approved by some other officer or directly handled by someone else.

Somebody else would have been in contact with Mr. Garman?

A. That is correct.

Q. You weren't personally involved in the signing of the documents or a discussion of the extensions, or the renewal notes, with Mr. Garman?

A. Would you rephrase that question?

Q. Were you personally involved—were you present when Mr. Garman executed any of these notes?

A. Not to my knowledge, but I could have been.

I know Mr. Garman and if—

The Court: There is no question pending, sir.

home by June 1, 1973, I have agreed to renew the loan to 9/15/73."

Then, it just says "credit account, checking account."

Q. Do you recall that being your instructions?

A. No, sir.

Q. And, there was no additional personal financial statement requested or received of Mr. Garman on March 2, 1973, is that correct?

A. I have no idea.

Q. You have—there is none introduced by you, nor do we know. To your knowledge, do you know whether you asked him or he was asked about it?

A. I have no idea.

By The Court:

Q. Were you in charge of Mr. Garman's account on that date?

A. No, sir.

Q. When had you left?

A. Around January 12th, the 15th, about the middle of January.

Q. of '73?

A. Yes, sir.

Q. Thank you.

December 21, 1971?

A. No, sir.

Q. Now, I believe you testified, Mr. Bishop, that in January of 1973, Mr. Garman was given the proceeds of an additional loan for $15,000, is that correct?

A. Yes, sir.

Q. And, in January, 1973, were you the officer who approved that loan, if you recall?

A. Yes, I believe I was.

Q. And, in January 15, 1973, did you ask for or receive from Mr. Garman an additional personal financial statement?

A. I asked for an additional personal financial statement.

Q. Did you receive one at that time?

A. No, sir.

Q. Prior to this loan?

A. No, sir.

Q. And at the time the proceeds of the loan were credited to Mr. Garman's account, January 15, 1973, did you have an additional personal financial statement from Mr. Garman?

A. No, I had one dated December 22nd.

Q. No, I asked you if you had one dated that date?

The Court: Not necessarily, if the proper foundation is made during the examination at the time, if it comes to pass, that the defendant goes ahead.

Then he could ask that they be admitted without Mr. Bishop being here.

Mr. Webb: I have allowed this witness to testify from the contents of these documents when they really aren't in evidence and I want to state for the record, I tend not to object so that it will make things speedier; I would ask the Court then to withhold ruling until Mr. Crane's chance to present his evidence when he can offer the exhibits and if they are relevant, it will not be necessary to call this witness back again.

The Court: All right.

So at this time, the Court will not rule on the admissibility of Defendant's Group Exhibit No. 11 or Defendant's Exhibit No. 12.

By Mr. Crane:

Q. Mr. Bishop, I call your attention to the loan made by Mr. Garman on December 21, 1971, about which you have testified.

Do you recall how much cash Mr. Garman was given at that time?

A. Would you repeat the date of that loan?

By The Court:

Q. As to this statement that was made on December 8, 1970, you said you looked back to the file for a couple of years, did you verify Mr. Garman's employment at that time?

A. No, sir, because I was familiar with the company and his superior in Chicago. I knew he was employed by that firm so I did not have to verify it.

Q. Did you verify how many dependents Mr. Garman had at that time?

A. No, sir. That was essentially irrelevant based on his income level and financial condition in terms of our loan.

Q. His net worth is the basis on which you make all of these decisions?

A. That coupled with the income, current indebtedness, in other words, his cash flow, his ability to repay the loan.

Q. All right. I am interested, and you will have to bear with me while I formulate some of these.

The cash flow shows $37,000. Is that gross income or net income?

A. That was the gross, I believe, yes, sir.

Q. You have to take out taxes from that?

A. Yes, living expenses and mortgage and so forth.

Q. Don't you come to some judgment, or some figure that you look to as to the monies that are available to repay any indebtedness?

A. Yes, sir.

Q. Did you, as to the December 8, 1970, statement?

A. Yes, sir.

Q. What was that figure?

I have a copy of here, that has been identified as Exhibit No. 2, you have $37,000 as total income?

A. Yes, sir.

Q. His net worth—I suppose what I am getting into, Mr. Bishop, the net worth here all seems to be tied up in a particular house?

A. Yes, sir, 39 from 75, the bulk of it.

Q. That is not very liquid?

A. No, sir, but with a $37,000 income, there should be sufficient monies to repay the loans.

Q. How much money do you think from that he had to repay the loans in 1970?

Why didn't you get a statement as to his monthly mortgage payment. It is not there, it it?

A. No, sir.

Q. What the school costs; do his children have school expenses?

A. That is an excellent idea.

Q. This is what I look to. I don't consider that necessarily a financial statement because it doesn't show the monthly income and expenses.

It may be a financial statement in the sense that it may be assets and liabilities, but somehow these are misleading, even if we assume that they were stated accurately as to what a cash position of a person is and what types of loans he can handle.

A. Of course, when we talk with a borrower, we set up a repayment schedule that meets his abilities that indicates quite a bit in terms of funds—

Q. These weren't monthly payments?

A. No, sir.

Q. It doesn't show that he has any cash on hand. He had an overdrawn checking account. So, where do you think the cash is going to come from to pay these loans?

A. His monthly or bimonthly payments from the company he works for.

Q. How do you know for any monthly or bimonthly payment that there would be funds available to pay the loan?

A. From the statement?

Q. Yes.

A. You can't tell from the statement.

Q. That's right.

The Court: Did you wish to ask Mr. Bishop any questions?

This bothers me on these types of statements.

Mr. Crane: Your Honor, may I recall Mr. Bishop later and ask just a few more questions?

You have asked him about the company that Mr. Garman is employed by which I think requires, for the benefit of the Court, an explanation from Mr. Bishop.

The Court: Why? I was just wondering if he verified this from the file or some other place, that is all.

It does bother me, Mr. Webb, and—Do we have any more quesions of Mr. Bishop?

Mr. Crane: I do.

The Court: Of what basis?

Mr. Crane: I would like Mr. Bishop to tell the Court what company Mr. Garman does work for.

The Court: New York Life. It says on the financial statement.

Mr. Crane: And whether New York Life is a major depositor in an account with the Northern Trust Company?

The Court: It may very well be.

statement one in the file that you reviewed before making or approving the November loan?

A. Yes.

Q. Or the renewal I should say?

A. Yes.

Q. To your knowledge, Ms. King, to this date, what is the amount of money due and owing by Mr. Garman as a result of loans he had from your bank?

A. $30,000.

Mr. Webb: I have no further questions, your Honor.

The Court: Do you have any questions, Mr. Crane?

Mr. Crane: Just a few, your Honor.

Cross-Examination by Mr. Crane.

Q. Now, Ms. King, on November 1, 1973, the date of that renewal note, did Mr. Garman receive any new cash?

A. No.

Q. Was this note signed at Mr. Garman's request or at your request?

A. Was the note signed at Mr. Garman's request or my request?

He would have to sign the note in order to renew the loan.

Q. Did you ask Mr. Garman to come in and renew the note because it was past due?

A. I don't remember.

Q. But, Mr. Garman didn't come in and ask to sign the new note for the same amount of money?

A. I don't remember.

Q. Would you, as a bank officer, have a note renewed that was unpaid for a period of six months?

A. Depending upon the circumstances of the loan, yes.

Q. Would it be to the bank's benefit to have this note renewed, November 1, 1973?

A. To the bank's benefit? Yes.

Q. Would that be required by the bank to have these notes renewed or brought up to date?

A. Yes.

Q. Would it be normal to request the borrower to come in and sign such a note if it hadn't been paid?

A. In most instances we just send the renewal note out for signing.

Q. As far as you know, this note wasn't signed at the request of Mr. Garman, was it?

A. No.

Q. Can I assume it was signed at the request of the bank?

A. Yes.

Q. Did you ever talk to Mr. Garman and ask him what his financial condition was in November, 1973?

A. I don't remember.

Q. Did you ever discuss Mr. Garman's financial condition with him at anytime?

A. Yes.

Q. When was that?

A. In May when I wrote him a letter and asked him for a financial statement.

By The Court:

Q. May of what year, please?

A. 1974. I didn't get a response and I telephoned him.

Q. That is after the due date of this note?

A. Yes.

By Mr. Crane:

Q. And, you never received the statement, is that correct?

A. I did not.

Mr. Crane: I have no further questions of this witness.

The Court: Do you have any further questions of this witness, Mr. Webb?

Mr. Crane: Will the Court permit a narrative answer from Mr. Garman?

Mr. Webb: I have no objection.

The Court: Mr. Webb controls the answers.

By Mr. Crane:

Q. Would you please explain what the nature of your relationship to Hal Solomon was and where that figure of $10,800 came from?

A. All right, fine.

That figure, first of all, these lists that Mr. Webb continually this afternoon referred to as my debts were in fact never debts with one exception, the case of the estate of Kenneth Stoen, where—

Q. What were they?

A. I signed the promissory note.

The reason it was not reflected on the bank's statement is because that was offset by stock which I own for Kenneth Stoen. So one offset the other and had nothing to do with the bank statement.

As to these others, I was instructed at the time when I was filing for bankruptcy and I had consulted with you and your firm, to list any possible indebtedness.

At that time, I actually didn't have these even in my mind. Then, after interrogating me further and we talked and talked for quite some length and you made a point of the fact that could there be possibly somebody who would claim, or make a claim against you because you made it clear that once I filed bankruptcy that I could never go back and say, "Hey, I forgot this."

So, on that recall, and with that in mind, I listed the potential and because it did say claim, that there were certain agreements that I had with these people that are listed here, informal agreements.

They were not legal documents; they were just informal agreements. However, they could be construed to be a claim.

In view of the fact that they could possibly become a claim in the future, I agreed to their listing on this form of bankruptcy.

I would like to reiterate without sounding disrespectful in any way, this was not intended to by-pass the question, but I wanted to make it clear that I did not hide anything.

I did not feel that the word "debt" did justice to what was involved here as the listing of a claim.

Incidentally, this form here says something where I signed it "to your information," and that was what I was referring to based on the information here that their statement of all my debts and all my property in acccordance to the best of my knowledge, information and belief, information being the information that you provided—

Q. Mr. Garman, may I interrupt you?

A. Yes.

Q. In Schedule A-3 you show the name Hal Solomon, MD?

A. Yes, sir.

Q. The amount of the claim approximately $10,800?

A. Yes, sir.

Q. Do you owe or do you think you owe Hal Solomon any money?

A. No.

Q. Did you think you owed Hal Solomon any money on the date that you prepared your bankruptcy schedule?

A. No, sir.

Q. What was your relationship with Hal Solomon?

A. Very close friend.

Q. Did he ever make a demand upon you for any money?

A. Never.

Q. Did he ever lend you any money?

A. No.

Q. What did the $10,800 figure represent?

A. It represented money that he had invested over a period of time with my counseling, that's where the counseling fees were listed on my statement with the bank.

I divulged that information to the bank that I was earning counselling fees advising some of these close friends on certain stock purchases.

It would be inconceivable that Dr. Solomon would make a claim against me, but it would be conceivable that it was

my advice that I gave him that maybe someone in his estate could possibly have filed a claim against me.

Q. Did Dr. Solomon purchase stock based on your recommendation?

A. Yes, he did.

Q. Were you to share in the profits of the sale of that stock?

A. Yes.

Q. And what if that stock did not make a profit but bore a loss?

A. We wiped out the losses before—

Q. Who is "we". When you made the arrangement with Dr. Solomon who was to bear that loss?

A. He would bear the loss and I would share, after losses were deducted, any gains would be shared.

Q. If the entire stock you recommended became worthless, would you be obligated to pay Dr. Solomon any money?

A. No, sir.

Q. Is this the same arrangement you had with Randolph Engler?

A. That is essentially the same arrangement, yes.

Q. Has Randolph Engler ever made any demand upon you?

A. No, sir.

Q. Is there any document in writing between yourself and Randolph Engler?

A. No, sir.

Q. Is that the same arrangement you had with Norman Isaacson?

A. Yes, sir.

Q. Has Norman Isaacson ever made a demand for payment?

A. No, sir.

Q. Are there any documents in writing between you and Norman Isaacson?

A. No, sir.

Q. Do you believe you owe Norman Isaacson any money?

A. Nothing.

Q. Did you at the time you filed and signed these financial statements to the Northern Trust?

A. No, sir.

Q. Did you at the time you prepared your bankruptcy schedule?

A. No, sir.

Q. Why did you list them in your bankruptcy schedule?

A. As I explained to you previously, sir, I was going by the claim, the word "claim" as a possible—

Q. Is it because I insisted you list them?

A. Yes, I didn't want to say that, but that's what it was.

I was trying to give myself credit for the claim part of it. I happen to be a student of semantics.

Q. Did you at any time ever consider these obligations of Hal Solomon, Norman Isaacson, and Randolph Engler or Kenneth Stoen debts of yours?

A. I made one exception to—

Q. Kenneth Stoen?

A. Mr. Stoen, that is correct.

Q. Did you consider these investments?

A. I considered this counseling, what my statement to the bank showed.

Q. When you refer to your statement to the bank, on all three financial statements referred to by Mr. Webb under the section "Annual Income," you have written in counseling fees?

A. That is correct.

Q. Are these the monies to be earned from the transactions with Mr. Solomon, Mr. Isaacson, and Mr. Engler?

A. That is correct.

Q. Did they ever ask you about the counseling fees?

A. Who?

Q. Did anybody at the bank ever ask you what counseling fees meant?

A. No, sir.

Q. Mr. Garman, were these financial statements true and correct? Did they truly reflect your assets and liabilities as of the date you prepared them?

A. I believe so.

Q. And, did your bankruptcy schedules truly reflect your assets and liabilities as of the date you prepared them?

A. Based on what you insisted on my putting down, I guess I would have to say yes, sir.

Q. Were you told you must put down every possible debt?

A. I don't know the words. You used more than possible, inconceivable, under the most unusual of all possibilities.

Mr. Crane: I have no further questions.

The Court: Do you have any other questions?

Mr. Webb: I have a couple of other questions.

I don't want to keep your Honor.

The Court: You keep going, I will watch the clock.

Examination

By Mr. Webb:

Q. Mr. Garman, in the deposition that I took of you, you referred to these matters as potential liabilities do you recall that?

A. That is correct.

Q. Now, you are referring to them as claims, is that correct?

A. If you have the words, I will have to say on one hand I referred to them as such and perhaps another—

The Court: Again, just listen to the questions.

The Witness: Yes, sir. He is asking me if I remember, and I don't remember.

The Court: If you don't remember say, "I don't